House Legislative Analysis Section
House Office Building, 9 South
Lansing, Michigan 48909
Phone: 517/373-6466

USE TAX PRESUMPTION: NO TAX AFTER 90 DAYS

House Bill 4219 (Substitute H-1)
First Analysis (3-20-03)

Sponsor: Rep. Gary Woronchak
Committee: Tax Policy

THE APPARENT PROBLEM:

The use tax is levied, generally speaking, on remote sales (such as those made through the Internet or mail order catalogues) and on out-of-state purchases of products that are then brought back into the state for storage, use, or consumption. The use tax is a companion to the sales tax and, like the sales tax, is levied at a rate of six percent. The taxpayer gets credit for taxes paid to other states (although not for taxes paid to other countries), so that a Michigan resident who purchases a product out of state and pays an equivalent amount of sales tax to that state is not liable for use tax in Michigan. If, for example, a person pays a four percent sales tax to another state, he or she would then be liable for a two percent use tax, representing the difference between the four percent tax in the other state and the six percent tax in Michigan.

As a practical matter, compliance with the use tax is considered "voluntary"; that is, it is self-reported by the taxpayer and the state has limited ability to enforce the tax. There is a line on the income tax form for taxpayers to use in reporting any use tax due on products purchased in the tax year. In some instances, however, the use tax can be routinely enforced. For example, automobiles, boats, or airplanes need to be registered in the state. In that case, the tax can be collected at the time of registration. This means a person cannot purchase an automobile in a state without a sales tax (such as New Hampshire or Montana) or with a sales tax lower than Michigan's (such as Alabama) and register it in Michigan without paying the required tax.

According to testimony before the House Tax Policy Committee, there appears to be no time limit on use tax liability. In a case provided to the committee, a person who moved to Michigan from Alabama was notified after registering her automobile that she needed to pay the difference between the tax rate in Alabama and the tax rate in Michigan, even though the automobile had been purchased several years earlier, and had been registered and used in the other state. Moreover, reportedly, the tax was on the purchase price of the vehicle and not its current value. This, apparently, is state tax policy.

The Use Tax Act contains a "presumption" that tangible personal property <u>is</u> subject to the tax if the property is brought into the state within 90 days of the purchase date and is considered as acquired for storage, use, or other consumption in Michigan. The act, however, does not contain a presumption that property brought into the state after 90 days is not subject to the tax.

In a recent court case, <u>Guardian Industries v the Department of Treasury</u> (November 2000), the Michigan Court of Appeals said, "There is no language in the statute that permits an exemption from taxation after the ninety-day period has expired". Essentially, the court said that the existence in statute of a presumption that property brought into the state within 90 days of purchase is intended for storage, use, or consumption in Michigan and is therefore taxable does not in and of itself lead to the presumption that property brought in after 90 days is not taxable. "The only effect of a presumption", the court said, "is to cast onto the opposite party the burden of going forward with proofs". The use tax presumption, in other words, puts the burden of proof on the taxpayer when property is brought into the state within 90 days of purchase. But when property is brought into the state more than 90 days after purchase, the use tax is still applicable since there is no language in the act providing otherwise. [Treasury officials say this court case affirmed rather than altered state tax policy.]

Some people believe this issue needs to be addressed to guard against Michigan residents being taxed on items long after they have been purchased and put to use.

THE CONTENT OF THE BILL:

House Bill 4219 would amend the Use Tax Act to add the presumption that tangible personal property is exempt from the use tax if brought into the state more than 90 days after the date of purchase and is not considered as acquired for storage, use, or other consumption in Michigan.

[The Use Tax Act currently states that "for the purpose of the proper administration of the act and to prevent evasion of the tax", it is presumed that tangible personal property is subject to the tax if the property is brought into the state within 90 days of the purchase date and is considered as acquired for storage, use, or other consumption in Michigan.]

MCL 205.93

FISCAL IMPLICATIONS:

The House Fiscal Agency says that the fiscal impact is difficult to determine, especially if the exemption is pursued aggressively by business. The HFA cites estimates from the Department of Treasury suggesting that the revenue loss could be at least $10 million per year and perhaps much more. One-third of use tax revenues are earmarked for the School Aid Fund, with the remainder going to the general fund. (HFA floor analysis dated 3-19-03)

ARGUMENTS:

For:

It seems unfair for people who move to Michigan from another state to be assessed use tax on automobiles (or other products) purchased years ago simply because the sales tax in that state was lower than the tax in Michigan. This bill would put an end to that practice by adding to the Use Tax Act a presumption that tangible personal property brought into the state more than 90 days after purchase was not taxable. The sponsor says this would apply only when a second test was met: that the property was not acquired for storage, use, or other consumption in this state. If these two tests are met, the property is presumed not to be taxable. Upon this interpretation, property acquired for storage, use, or consumption in Michigan would not be exempt. Note that the bill does not, strictly speaking, provide an exemption from taxation. It provides a presumption, which puts the burden of proof that property is taxable onto the Department of Treasury. This is where the burden belongs. The new presumption is a companion to the current presumption in the act that property brought into the state within 90 days of purchase is taxable. This seems a reasonable approach. The current use tax law turns many Michigan residents into inadvertent tax cheats (because they theoretically owe tax that as a practical matter cannot be collected unless paid voluntarily). This is intolerable.

Response:

The bill is overly broad. A more narrowly drawn bill could prevent the case of the automobile purchased by a person then resident in another state being taxed upon registration in Michigan (and could prevent the threat of taxation of other personal property brought to the state by a new resident). This bill seems to do far more: it appears to provide a presumption that goods purchased outside the state are not taxable if not brought into the state until more than 90 days after purchase. Would this permit a Michigan resident or a Michigan business to escape taxation by purchasing a product in a state without a sales tax, leaving it in that state for a little over three months, and then bringing it into Michigan? If so (and some argue that is the effect), that is a large loophole that hurts not only the revenues of state government but could also hurt the sales of Michigan firms if they lose customers to businesses in other states. Note that in the Guardian Industries v Michigan Department of Treasury case, the issue was a $19 million dollar airplane on which use tax of about $760,000 was paid. (This occurred in 1989 when the tax rate was at four percent.) This issue is about more than used Hondas. Whether tax is due on property brought into the state after 90 days should be based on the facts in each case; there should be no presumption to hobble or frustrate the Department of Treasury. This bill creates an unworkable test, according to treasury officials.

Against:

The bill has significant revenue implications, perhaps in the tens of millions of dollars. Treasury officials have said it could cost the state as much as $60 million. This is because it has the potential to create a loophole that could be exploited to allow many transactions that are now taxable to escape taxation. About one-third of the lost revenue will be lost to the School Aid Fund. This is hardly the time, with severe budget cuts ahead for many valuable state programs, to enact legislation that could have serious negative fiscal consequences for the state.

Response:

Some people believe the estimates of potential revenue loss are greatly exaggerated. They also question how the state can argue that it cannot provide tax fairness, cannot rectify obviously unfair tax policies, because of budget difficulties. It is not reasonable to say that a glaring weakness in state tax policy can only be addressed when more money becomes available.

POSITIONS:

The Department of Treasury is opposed to the bill. (3-19-03)

The Michigan Education Association is opposed to the bill. (3-19-03)

Analyst: C. Couch

■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.