

Legislative Analysis



SALES AND USE TAXES: DELIVERY CHARGES

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House Bill 6089 as introduced
Sponsor: Rep. Jerry O. Kooiman

House Bill 6090 as introduced
Sponsor: Rep. Glenn Steil, Jr.

Committee: Tax Policy
First Analysis (6-12-06)

BRIEF SUMMARY: The bills would amend the General Sales Tax and Use Tax Acts to exempt from taxation delivery charges from direct mail if those charges are separately stated on an invoice or similar billing documents given to the purchaser.

FISCAL IMPACT: The bills would reduce sales and use by a relatively small amount. The combined impact would probably be less than \$1.0 million.

THE APPARENT PROBLEM:

Under the General Sales and Use Tax Acts, delivery charges (including postage) incurred or to be incurred before the property is transferred from the seller to the buyer are subject to taxation. Currently, there is some confusion over the taxability of delivery charges (postage) of direct mail printing and advertising firms. Generally speaking, direct mail advertising firms create and design advertising campaigns for the purpose of distributing advertising materials (e.g. coupons, credit card solicitations, and flyers) by mail or other direct distribution. These firms also prepare advertising materials for mailing or other direct distribution by folding and placing the material in an envelope, affixing postage, and sorting items by zip code. Additionally, commercial printers also print a variety of materials (billing statements, brochures, flyers) and directly mail these materials for their customers. Generally, the cost of postage incurred by these firms on behalf of the customers is cheaper than if the customer were to mail because the direct mail firm can use its postal permit enabling it to mail items at a discount.

Historically, these direct mail firms have not paid sales and use taxes on the cost of postage, even though there appears to have been no such exemption in state tax law.¹ It also appears that the Department of Treasury has not enforced collection of the tax until recently, following recent amendments made to the sales and use tax acts under the Streamlined Sales

¹ Rule 74 of the General and Specific Sales and Use Tax Rules (R 205.124) states: "[f]or the purpose of computing the tax, no deduction is allowable on account of freight, express, mail, cartage, or other transportation or delivery charges incurred or to be incurred on tangible personal property prior to completion of transfer of ownership of such property from the seller to the purchaser for use or consumption. It is immaterial whether such transportation charges are billed separately or whether they are paid by the seller or purchaser." Further, the General Sales Tax Act, prior to recent amendments, defined "gross proceeds" to mean "the amount of received in money, credits, subsidies, property, or other money's worth in consideration of a sale at retail within this state, without a deduction for the cost of the property sold, the cost of material used, the cost of labor or serviced purchased...or other expenses."

Tax Project (see Public Acts 172 and 173 of 2004). The streamlined sales and use tax agreement agreed to by the states specifically includes delivery charges within the base of the sales and use taxes. When first agreed to, many states either did not impose sales and use taxes on delivery charges or, if they did, exempted direct mail from taxation. Recognizing this, the agreement permits states to exempt delivery charges or, if they tax those charges, to exempt direct mail charges that are separately stated on an invoice or similar document given to the purchaser. Many states have opted to continue the exemptions, either at the time they enacted legislation conforming to the agreement or by enacting subsequent legislation specifically exempting such charges. Public Acts 152 and 153 do not currently exempt these charges.

Representatives of the printing industry are concerned that direct mail charges will now be subject to taxation. They contend that the imposition of the tax or, perhaps more accurately stated, the enforcement of the tax, including the payment of back taxes, will "devastate" the direct mail industry within the state, placing firms at an economic disadvantage with firms located in states where such charges are not subject to taxation.

THE CONTENT OF THE BILL:

House Bills 6089 and 6090 would amend the Use Tax Act (MCL 205.92b) and General Sales Tax Act (MCL 205.51a), respectively, to specify that beginning September 1, 2004, "delivery charges" do not include the charges for delivery of direct mail if the charges are separately stated on an invoice or similar billing document given to the purchaser.

Delivery charges are included within the definition of "purchase price" within the Use Tax Act and within the definition of "sales price" in the General Sales Tax Act, and so make up part of the base for each of those taxes.

The acts define "delivery charge" to mean charges by the seller for preparation and delivery to a location designated by the purchaser of tangible personal property or services. Delivery charges include, but are not limited to, transportation, shipping, postage, handling, crating, and packing.

The acts define "direct mail" to mean printed material delivered or distributed by United States mail or other delivery service to a mass audience or to addresses on a mailing list provided by the purchaser or at the direction of the purchaser when the cost of the items is not billed directly to the recipients, including tangible personal property supplied directly or indirectly by the purchaser to the direct mail seller for inclusion in the package containing the printed material but not including multiple items of printed material delivered to a single address.

BACKGROUND INFORMATION:

Use Tax Act

The Use Tax Act (MCL 205.92) defines "purchase price" or "price" to mean the total amount of consideration paid by the consumer to the seller, including cash, credit, property, and services, for which tangible personal property or services are sold, leased, or rented, valued in money, whether received in money or otherwise, and applies to the measure subject to use

tax. Purchase price includes delivery charges incurred or to be incurred before the completion of the transfer of ownership of tangible personal property from the seller to the purchaser.

General Sales Tax Act

The General Sales Tax Act (MCL 205.51) defines "sales price" to mean the total amount of consideration, including cash, credit, property, and services, for which tangible personal property or services are sold, leased, or rented, valued in money, whether received in money or otherwise, and applies to the measure subject to sales tax. Sales price includes delivery charges incurred or to be incurred before the completion of the transfer of ownership of tangible personal property from the seller to the purchaser.

Examples

The following examples demonstrate when postage costs would be subject to taxation, and are based on a recent letter ruling from the Department of Treasury.

The basic facts: Company A receives an order from Customer Z for the printing and mailing of medical statements. Customer Z provides patient data necessary for the bill.

- Company A prints the statements on letterhead and envelopes that are provided by Customer Z. Company A mails the statements using its own postal permit, and passes the cost of postage to Customer Z. *This transaction is considered a service and is, therefore, not subject to sales tax.*
- Company A prints the statement on letterhead and envelopes that it provides. This transaction is considered to be a sale subject to taxation, and tax is paid on the "sales price," which includes postage.
- Company A prints the statements on letterhead and envelopes that Customer Z provides, and mails the statements and purchases postage using the postal permit of Customer Z. *This transaction is considered a service and is, therefore, not subject to sales tax.*
- Company A prints the statement on letterhead and envelopes it provides, and mails the statements using the postal permit of Customer Z. *The transaction is subject to sales tax, but postage is not taxed because the postal permit is owned by Customer Z.*
- Company A prints the statements on letterhead and envelopes it provides, and mails the statements using its own postal permit. Company A provides Customer Z with two invoices, one for the costs for printing and stuffing the envelopes and the other for the amount of postage. *This transaction is subject to sales tax. The "sales price" includes postage, and it is immaterial that postage is stated on a separate invoice.*
- Company A mails medical statements of Customer Z, which has the statements printed from a company outside of Michigan. The statements are drop shipped to Company A, which prepares the statements for mailing and mails them using its own

postal permit. *This transaction is considered a service and is, therefore, not subject to sales tax.*

ARGUMENTS:

For:

In essence, the bills codify what apparently has been a long standing practice of the direct mail industry and the Department of Treasury. Direct mail firms have stated that they have never paid sales tax on the cost of postage, and that the department historically has not enforced collection of the tax. Reportedly, some firms have recently been subject to a sales and use tax audit, and this issue was never raised. Moreover, the industry generally does not consider the amount of postage charged to customers to be part of the cost of providing the service, as they merely pass their postage costs on to the customer without a markup. There is no profit made.

The exemption is particularly beneficial to smaller printers which typically do not have a postal permit enabling them to mail items at a discount. Postage paid by printers using their own postal permits (typically larger ones) is not subject to sales tax. By exempting postage, the bill treats printers, large and small, in the same manner.

Finally, it should be added many contend that the imposing the sales tax on postage (an obligation of the federal government) violates federal law. In 1996, the Mississippi Supreme Court ruled in *H.J. Wilson v. State Tax Commission of the State of Mississippi* that the imposition of the sales and use taxes on postage used to calculate taxable delivery charges violates the federal Public Debt Act of 1941 (31 USC 3124), which exempts stocks and obligations of the U.S. government, including "stamps and other representatives of value," from taxation by the state or a political subdivision of the state.

Response:

To the argument that the tax violates federal law, it should be stated that the tax is not a direct tax on postage. The transaction subject to tax is between the direct mail firm and its customer, not on the direct mail firm's purchase of postage from the U.S. government.

POSITIONS:

Printing Industries of Michigan, Inc. supports the bills. (6-7-06)

The Department of Treasury has no position on the bills. (6-7-06)

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■ 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.