



Senate Fiscal Agency
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BILL



ANALYSIS

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Senate Bill 624 (Substitute S-1 as passed by the Senate)

(as enrolled)

House Bill 4930 (Substitute H-1 as passed by the Senate)

(as enrolled)

Sponsor: Senator Jason E. Allen (S.B. 624)

Representative Kate Segal (H.B. 4930)

Senate Committee: Finance

House Committee: New Economy and Quality of Life (H.B. 4930)

Date Completed: 6-12-09

RATIONALE

Public Acts 17 and 18 of 2006 amended the General Sales Tax Act and the Use Tax Act, respectively, to create tax exemptions for the sale of parts and materials affixed to aircraft that are temporarily within Michigan, and for the sale of aircraft that are temporarily located in the State for certain purposes. For the sale of an aircraft to be exempt, it must be in the State for the purpose of prepurchase evaluation (an examination to give a potential purchaser relevant information) or prepurchase evaluation and postsale customization. The tax exemptions were enacted to assist a Battle Creek company, Duncan Aviation, which refurbishes and customizes airplanes in addition to performing prepurchase evaluations. Typically, when planes are flown into Michigan for these purposes and then sold, the sales take place in this State. There were concerns that, without the exemptions, Duncan's clients could have taken their business to another state where the transactions would be tax exempt. The language of the amendments target used aircraft, however, which is what Duncan originally worked on. Now, the company evidently has potential clients who would like to have new aircraft customized, and concerns about out-of-State competition again have been raised. It has been suggested that the tax exemptions should be broadened to cover new aircraft sales, in order to retain this business activity in Michigan.

CONTENT

Senate Bill 624 (S-1) would amend the Use Tax Act and House Bill 4930 (H-1) would amend the General Sales Tax Act to revise tax exemptions for the sale of aircraft that are temporarily in this State, by deleting language that limits the exemptions to used aircraft.

Currently, if specific conditions are met, the use tax and the sales tax do not apply to the sale of an aircraft temporarily located in Michigan for the purpose of prepurchase evaluation or for prepurchase evaluation and postsale customization. The bills, instead, would exempt from the taxes the sale of an aircraft temporarily in the State for the purpose of a sale and prepurchase evaluation, customization, improvement, maintenance, or repair.

Under the conditions that presently must be met, the aircraft must leave this State within 15 days after authorized approval for final return to service, completion of the maintenance record entry, and completion of the test flight and ground test for inspection as required by 14 CFR 91.407 (which prohibits a person from operating any aircraft that has undergone maintenance, rebuilding, or alteration unless it has been approved for return to service by an authorized person and a required maintenance record entry has been made). The bills would delete this language. Instead, the bills would require the aircraft to leave the State within 15 days after the

sale and completion of any prepurchase evaluation, customization, or improvement, maintenance, or repair associated with the sale, whichever was later.

In addition, under the Acts, the aircraft may not be based or registered in this State before or after the prepurchase evaluation or the prepurchase evaluation and postsale customization are completed. Under the bills, the aircraft could not be based or registered in the State before or after the sale and completion of any prepurchase evaluation, customization, improvement, maintenance, or repair associated with the sale.

Both bills would define "customization" as any improvement, maintenance, or repair that is performed on an aircraft that is associated with the sale of the aircraft.

Both bills would have to be applied retroactively to transactions occurring after June 11, 2009.

MCL 205.94k (S.B. 624)
205.54x (H.B. 4930)

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The tax exemptions enacted in 2006 have contributed to the success of Duncan Aviation and the retention of jobs in Michigan. According to the company's website, Duncan has a 325,000-square-foot facility in Battle Creek, where it employs 675 individuals; in 2008, this facility was voted the number two avionics shop and the number four maintenance shop in the United States in the annual *Professional Pilot* survey. When the tax exemptions were enacted, Duncan performed prepurchase inspections, which involve taking a used plane apart, and refurbished used aircraft. Now, the company has a potential seven-year contract to customize 23 new aircraft. Unless the tax exemptions are broadened, the sale of these planes in Michigan will be subject to the State's sales and use taxes, which could amount to a liability of several million dollars per plane.

Considering the mobility of the product, Duncan's potential clients could very easily take their business to another state or country where the transactions would be tax exempt. Duncan Aviation, in fact, is based in Lincoln, Nebraska, which has a "fly-away" tax exemption. Thus, the company itself could retain the business, but the Michigan facility would lose it. Although only a handful of other firms perform the type of work that Duncan does, 25 or 26 other states have comparable tax exemptions.

These bills are necessary for both Michigan and Duncan Aviation's Battle Creek facility to compete successfully and keep jobs in this State. In addition to helping Duncan, the bills would benefit other Michigan companies that work on new aircraft, and would promote economic diversity in Michigan.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

Under current law, new aircraft brought into Michigan by an out-of-State or foreign manufacturer to have custom finishing work done on the aircraft would be subject to Michigan's sales or use tax if the manufacturer of the aircraft finalized the sale and the new owner took possession of the aircraft in Michigan. This type of work has not been conducted in Michigan in the past, so no sales or use tax has been collected from this type of business activity before; however, at least one Michigan business is just beginning to conduct finishing work on new aircraft, including the installation of customized interiors. Whether the sale of these new aircraft is taxed by a state is important because when a new aircraft is finished at a different site from where it is manufactured, it is frequently convenient and cost effective to have the manufacturer finalize the sale and have the new owner take possession of the aircraft where it is finished, instead of incurring the additional cost of moving it back to the manufacturer's location.

Under current law, finalizing the sale of these new aircraft in Michigan would result in a \$3.0 million to \$4.0 million sales tax liability per aircraft, which is an added expense that both the manufacturer and new owner would want to avoid and would be able to avoid in two ways: 1) The finished

aircraft could be moved to another state that exempts this type of transaction from its sales tax and the sale of the aircraft could be finalized in this other state, or 2) the customization work could be done in another state where the sale could be finalized without producing any sales tax liability. Currently, about 26 other states provide such a sales tax exemption on new aircraft. Therefore, given that no Michigan sales tax revenue has been collected from this type of business activity in the past and that out-of-State aircraft manufacturers would likely take actions to avoid Michigan's sales tax by either moving the finished aircraft to another state to finalize the sale or having the finishing customization work done in another state that would allow the eventual sale to be tax exempt, it is estimated that these bills would have no fiscal impact on sales or use tax revenue.

Fiscal Analyst: Jay Wortley

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.