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BILL ANALYSIS

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Senate Bill 337 (as enacted) **PUBLIC ACT 3 of 2014**
Sponsor: Senator Jack Brandenburg
Senate Committee: Finance
House Committee: Tax Policy

Date Completed: 3-3-14

CONTENT

The bill amended the revenue Act to do the following:

- **-- Set deadlines for the Department of Treasury, when conducting an audit, to complete fieldwork, provide a preliminary audit determination to the taxpayer, and issue a final assessment.**
- **-- Revise and expand the circumstances in which the statute of limitations must be extended.**
- **-- Allow a taxpayer to treat a claim for a refund as denied, and bring an appeal, if the claim has not been approved, adjusted, or denied within one year.**

The bill also amended provisions of the Act under which the purchaser of a business may be liable for the former owner's unpaid taxes, to do the following:

- **-- Require the Department to release the business's known or estimated tax liability to the purchaser within 60 days of a request, if the owner waives confidentiality.**
- **-- Limit the purchaser's liability to the known or estimated tax liability disclosed by the Department, if the purchaser complies with escrow requirements.**
- **-- Provide that the purchaser cannot be held liable if the Department does not comply with the disclosure requirement.**

In addition, the bill amended provisions that make an officer, manager, or partner personally liable for unpaid taxes of a business, to do the following:

- **-- Limit personal liability to a "responsible person", i.e., a person who was responsible for filing returns or paying taxes during the time period of default, and willfully failed to file or pay.**
- **-- Prohibit the Department from assessing a responsible person more than four years after the date of the assessment issued to the business.**
- **-- Provide that the Department has the burden of producing prima facie evidence or establishing a prima facie case that a person is a responsible person.**
- **-- Require the Department to notify the responsible person of amounts collected from another responsible person or a business purchaser attributable to the assessment.**
- **-- Require the Department to assess a purchaser of the business before assessing a responsible person, under certain circumstances.**
- **-- Require the Department to disclose various documents to a responsible person.**

-- **Allow a responsible person to challenge an assessment to the same extent the business could have done.**
-- **Allow a responsible person to recover from another responsible person in a circuit court proceeding.**
-- **List the taxes for which a responsible person may be personally liable.**

The bill took effect on February 6, 2014.

Audit Deadlines

The Act allows the Department to obtain information for the assessment of a tax when a taxpayer fails or refuses to make a return or payment as required, or when the Department believes that a return or payment does not supply enough information for an accurate determination of the amount due. Through its agents, the Department may examine the books, records, and papers, and audit the accounts of a person or any other records pertaining to the tax.

In carrying out these responsibilities, the Department must send the taxpayer a letter of inquiry, except in certain situations. If the dispute is not resolved within 30 days after the letter is sent, or if a letter is not required, the Department must give the taxpayer notice of its intent to assess the tax. If the taxpayer serves written notice on the Department within 60 days after receiving the letter, pays the uncontested portion of the liability, and provides a statement of contested amounts and an explanation of the dispute, the taxpayer is entitled to an informal conference on the question of liability for the assessment. After the informal conference, the Department must render a decision and order, and assess the tax, interest, and penalty found to be due. If the taxpayer does not protest the notice of intent within the time provided, the Department may assess the tax, interest, and penalty; this assessment is final and may be appealed to the Tax Tribunal or the Court of Claims.

Under the bill, the following requirements apply to audits commenced after September 30, 2014.

The Department must complete fieldwork and provide a written preliminary audit determination for any tax period within one year after the four-year statute of limitations provided for in Section 27a(2). This requirement does not apply to any tax period in which the Department and the taxpayer agreed in writing to extend the statute of limitations. (Section 27a(2) prescribes a four-year period, referred to as the statute of limitations, for a taxpayer to claim a refund after the date set for filing the original return; or for the Department to assess a deficiency, interest, or a penalty after the filing date or the date a return was filed.)

Unless otherwise agreed to by the taxpayer and the Department, the final assessment must be issued within nine months of the date the Department provided the taxpayer with a written preliminary audit determination, unless the taxpayer, for any reason, requests reconsideration of the preliminary audit determination or requests an informal conference. A taxpayer's request for reconsideration permits, but does not require, the Department to delay issuing a final assessment.

Extension of Statute of Limitations

Previously, the Act provided for running of the statute of limitations to be suspended for the following:

-- The period pending a final determination of tax, including audit, conference, hearing, and litigation of liability for Federal income tax or a tax administered by the Department, and for one year after that period.

-- The period for which the taxpayer and the State consented to the extension.

Under the bill, instead, the statute of limitations must be extended for the following if the period exceeds the four-year period set in Section 27a(2):

-- The period pending a final determination of tax through audit, conference, hearing, and litigation for Federal income tax, and for one year after that period.
-- The period for which the taxpayer and the State have consented to the extension.
-- The periods established by the bill for a preliminary audit determination and a final assessment (described above), or pending the completion of an appeal of a final assessment.
-- A period of 90 days after a decision and order from an informal conference, or a court order that finally resolves an appeal of a decision of the Department in a case in which a final assessment was not issued before appeal.

As previously provided, the statute of limitations is extended only as to those items that were the subject of the audit, conference, hearing, or litigation. The bill defines "items that were the subject of the audit" as items that share a common characteristic that were examined by an auditor even if there was no adjustment to the tax as a result of the examination. Items that share a common characteristic include items that are reported on the same line on a tax return or items that a grouped by ledger, account, or record or by class or type of asset, liability, income, or expense.

<u>Liability of Purchaser of a Business</u>

Under the Act, a person who purchases a going or closed business, or its stock, is required to escrow enough money to cover the amount of taxes, interest, and penalties that may be due and unpaid, until the former owner produces a receipt from the State Treasurer showing that the taxes are paid, or a certificate stating that the taxes are not due.

Previously, if the owner waived confidentiality, the Department was permitted to release to the purchaser the business's known tax liability for the purpose of establishing the escrow account. The bill instead requires the Department, within 60 days of receiving the request, to timely release the business's known or estimated liability, if the owner waives confidentiality.

The bill allows the Department to estimate tax liability based on prior returns and payments. If it believes that a return or payment does not supply enough information for an accurate determination, the Department may make an estimate based on other available information.

Under the Act, if the purchaser or a succeeding purchaser fails to comply with these escrow requirements, the purchaser is personally liable for the payment of the taxes, interest, and penalties accrued and unpaid by the business of the former owner. The bill specifies that, if the purchaser or succeeding purchaser complies with the escrow requirements, the purchaser cannot be held liable for more than the known or estimated tax liability disclosed by the Department and held in escrow. The purchaser cannot be held liable, however, if the Department has failed to provide the information requested within 60 days.

For a purchaser or succeeding purchaser that has not complied with the escrow requirements, the purchaser's liability is limited to the fair market value of the business less the amount of any proceeds that are applied to balances on certain secured transactions. (The Act previously contained this limitation but it was not restricted to purchasers who did not comply with the escrow requirements.)

Personal Liability for Business Default

Liability of Responsible Person. Previously, if a business (a corporation, limited liability company, limited liability partnership, partnership, or limited partnership) was liable for taxes administered under the Act and failed, for any reason, to file required returns or pay a tax due, any of its officers, members, managers, or partners was personally liable for the failure, if the Department of Treasury determined, based on an audit or investigation, that he or she had control or supervision of, or responsibility for, making the returns or payments.

Under the bill, in such a situation, an officer, member, manager of a manager-managed limited liability company (LLC), or partner is personally liable if he or she is a "responsible person" and fails, for any reason after assessment, to file the required returns or pay the tax due. "Responsible person" means an officer, member, manager of a manager-managed LLC, or partner for the business who controlled, supervised, or was responsible for the filing of returns or payment of any of the taxes listed in the bill during the time period of default and who, during that period, willfully failed to file a return or pay the tax due.

("Time period of default" means the tax period for which the business failed to file the return or pay the tax due and through the date set for filing the return or making the required payment, whichever is later. "Willfully" means the person knew or had reason to know of the obligation to file a return or pay the tax, but intentionally or recklessly failed to do so.)

The bill prohibits the Department from assessing a responsible person more than four years after the date of the assessment issued to the business.

Collection from Other Responsible Person or Purchaser. The bill requires the Department to provide a responsible person assessed under these provisions with notice of any amount collected by the Department from any other responsible person or purchaser of the business determined to be liable, that is attributable to the assessment.

A responsible person may challenge the validity of an assessment to the same extent that the business could have done when the assessment was originally issued. The Department has the burden to first produce prima facie evidence (as described below) or establish a prima facie case that the person is the responsible person through establishing all elements of a responsible person as defined in the bill.

In a separate proceeding before the circuit court, a responsible person found to be liable for the assessment may recover from other responsible persons an amount equal to the assessment or portion of the assessment based on that person's proportionate liability for the assessment, as determined in that proceeding.

Before assessing a responsible person as liable for the tax assessed to the business, the Department must first assess a purchaser or succeeding purchaser of the business personally liable under the Act if the Department has information that clearly identifies a purchaser and establishes that the assessment of the purchaser would permit the Department to collect the entire amount of the tax assessment of the business. Notwithstanding the liability of a purchaser, the Department may assess a responsible person if the purchaser fails to pay the assessment.

Signature as Prima Facie Evidence. Previously, the signature of an officer, member, manager, or partner on returns or negotiable instruments submitted in payment of taxes was prima facie evidence of the responsibility for making the returns and payments. (Prima facie evidence is evidence sufficient to establish a given fact or raise a presumption unless disproved or rebutted.)

Under the bill, the signature, including electronic signature, of an officer, member, manager of a manager-managed LLC, or partner on returns or negotiable instruments submitted in payment of taxes of the business during the period of default, is prima facie evidence that the person is a responsible person. A signature on a return or negotiable instrument submitted after the period of default is not prima facie evidence that the person is a responsible person for that period but may be considered along with other evidence to make a prima facie case that the person is a responsible person.

With respect to a return or negotiable instrument submitted before the time period of default, the signature on that document along with other evidence sufficient to demonstrate that the signatory was an officer, member, manager of a manager-managed LLC, or partner during the time period of default is prima facie evidence that the person is a responsible person.

Disclosure of Documents. Upon the request of a responsible person who was issued an intent to assess by the Department for a business's liability, the bill requires the Department to disclose any documents considered in its audit or investigation in determining that the person is a responsible person and is personally liable for the assessment, and any other documents that the tribunal or court determines are necessary for a fair adjudication of a person's liability under these provisions.

Taxes. Under the bill, for assessments issued to a responsible person before January 1, 2014, the provisions for personal liability apply to taxes administered under the Act. For assessments issued to a responsible person after December 31, 2013, the provisions apply to all of the following:

-- Taxes levied under the General Sales Tax Act.
-- Taxes levied under the Use Tax Act.
-- Taxes levied under the Tobacco Products Tax Act.
-- Taxes levied under the Motor Fuel Tax Act.
-- Taxes levied under the Motor Carrier Fuel Tax Act.
-- Withholding and remittance of income taxes under the Income Tax Act.
-- Any other tax administered under the revenue Act that a person is required to collect from or on behalf of a third person, to truthfully account for and to pay over to the State.

Claims for Refunds

The Act allows a taxpayer, within the statute of limitations, to petition the Department for a refund of a tax that the taxpayer paid but claims is not due.

Under the bill, if a claim for a refund has not been approved, denied, or adjusted within one year of the date it was received, the taxpayer may treat the claim as denied and may appeal it in accordance with Section 22. This does not apply to a claim for a refund under Part 1 of the Income Tax Act (which provides for the individual income tax.)

(Section 22 of the revenue Act allows a taxpayer to appeal the contested portion of an assessment, decision, or order to the Tax Tribunal within 35 days, or to the Court of Claims within 90 days, after the assessment, decision, or order. The uncontested portion of an assessment, order, or decision must be paid as a prerequisite to appeal. The taxpayer or the Department may appeal by right the decision of the Tax Tribunal or Court of Claims to the Court of Appeals.)

MCL 205.21 et al. Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill will have an indeterminate effect on the operations costs of the Department of Treasury and State revenue. The new 60-day requirement to release certain tax information will increase the Department's costs. The release of taxpayer liability if the Department fails to meet the timeline, and the limitations placed in the definition of the responsible party from whom unpaid tax liabilities may be collected, potentially will reduce State revenue. The one-year timeline on Treasury decisions regarding taxpayer refunds will permit some taxpayers to pursue appeals with the Tax Tribunal or the Court of Claims. This will have an unknown impact on State revenue.

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