Legislative Analysis

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SALES, USE, AND PERSONAL PROPERTY TAXES: EXEMPTIONS FOR DATA CENTERS

Senate Bill 616 (reported from House committee as H-1)
Sponsor: Sen. Tonya Schuitmaker

Senate Bill 617 (reported as H-1)
Sponsor: Sen. Peter MacGregor

Senate Bill 618 (reported as H-1)
Sponsor: Sen. Dave Hildenbrand

Senate Committee: Michigan Competitiveness
House Committee: Tax Policy
Complete to 12-11-15

SUMMARY:

The bills would amend various acts to exempt certain personal property associated with the operation of a qualified data center from sales, use, and property taxes. The sales and use tax exemptions would apply from January 1, 2016, to December 31, 2035. The property tax exemption would apply from December 31, 2015, to December 31, 2035.

<u>Senate Bills 616 and 617</u> would provide for an exemption from both the sales tax and the use tax for data center equipment, or the storage, use, or consumption of data center equipment, sold to the owner or operator of a qualified data center or a colocated business for use or consumption in the operations of the data center.

Further, Senate Bills 616 and 617 would require the legislature to annually appropriate sufficient funds from the state's General Fund to the State School Aid Fund to fully compensate for any loss of revenue to the SAF from the sales tax exemption.

Senate Bill 616 would amend the General Sales Tax Act (MCL 211.9p). Senate Bill 617 would amend the Use Tax Act (MCL 205.104b, et al.).

<u>Senate Bill 618</u> amends the General Property Tax Act (MCL 211.19 et al.) to provide for an exemption for eligible data center personal property, if the local tax collecting unit and the county approved the exemption request for a new data center or did not reject the exemption request for an existing data center.

Qualified Data Centers. A qualified data center is defined in each of the bills as a facility composed of one or more buildings located in Michigan and that is owned or operated by an entity whose "primary business" is owning, operating, managing, or maintaining a group of networked computers or networked facilities for the purpose of centralizing, or allowing one or more colocated businesses to centralize, the storage, processing, management, or dissemination of data of one or more other persons or the data of a colocated business. The term "primary business" means at least 75% of the entity's business activity.

Data Center Equipment. Senate Bills 616 and 617 would exempt data center equipment from the sales and use tax, and the bills define such equipment as high-technology equipment consumed or used physically within a qualified data center, including but not limited to computers, servers, routers, switches, peripheral computer devices and their associated tools, racks, shelving, cabling, and wiring. ("High technology" would mean technology used in the creation, storage, processing, or manipulation of digital data.)

The term also would include any construction materials used or assembled under the qualified data center's proprietary method, including but not limited to building materials, infrastructure, machinery, wiring, cabling, devices, tools, and equipment that would otherwise be considered a fixture or related equipment.

The term also applies to storage batteries, back-up generators, uninterrupted power supply units, and other redundant power supply equipment. The term would not include any equipment owned by a third party that is used to supply the data center's primary power.

Colocated Business. In each of the bills, a colocated business is defined as a person that enters into a contract with the owner or operator of a qualified data center to deploy or use data center equipment physically located within the data center for one or more years. Senate Bill 618 additionally requires the business to physically use or occupy all or part of the qualified data center for a period of one or more years for the purposes of centralizing the storage, management, and dissemination of the colocated business' data.

Property Tax Exemption. The property tax exemption applies to eligible data center property and can be claimed only by a person that owns the eligible data center property and that owns, leases, or otherwise physically uses or occupies all or part of the qualified data center in which the property is located. This includes, but is not limited to, a colocated business.

Eligible Data Center Property. Senate Bill 618 would define "eligible data center property" as all commercial personal property and industrial personal property purchase on or after December 31, 2015, that is directly used to operate, maintain, manage, or support the business of that qualified data center or a colocated business that physically uses or occupies all or part of the qualified data center.

Local Option for Property Tax Exemption. The property tax exemption is subject to one of the following conditions:

- For eligible data center property in a qualified data center <u>in operation before January 1, 2016</u>, the exemption is only available if it is requested in writing no later than February 1, 2016, and if the governing bodies of the local tax collecting unit and county where the qualified data center is located fail to adopt resolutions rejecting the request before May 1, 2016.

- For eligible data center property in a qualified data center <u>that begins operation after December 31, 2015</u>, the exemption is available only if it is requested in writing no later than February 1 of the first year the eligible data center property would be subject to taxes without the exemption, and if the governing bodies of the local tax collecting unit and county adopt resolutions approving the exemption request before May 1 of that year.

FISCAL IMPACT:

The package as a whole would reduce sales tax, use tax, and personal property tax revenue by an indeterminate amount. There are currently about 40 data centers operating in Michigan that would become eligible for the exemptions. Based on information from the Annual Capital Expenditures Survey (U.S. Census Bureau) corresponding to data centers at the national level, the resulting annual decline in sales and use taxes would be about $13.0 million, and the corresponding annual reduction in personal property revenue would be roughly $12.0 million assuming that local units of government do not reject the exemptions for the existing personal property.

However, this estimate does not include revenue losses associated with the colocated businesses that would also qualify for the preferential tax treatment, nor does it account for the possibility that existing businesses could spin off their data collection departments into subsidiaries and colocate as a way to qualify. The extent to which this would result in additional revenue reduction cannot be determined from available information.

In addition, no attempt has been made to estimate any revenue losses that would occur as data centers open or expand in Michigan because the amount of potential new investment and the corresponding time frame cannot be known in advance. However, as a point of reference, exempting $1.0 billion of capital expenditures from sales/use taxes (assuming 75% of the investment is tangible personal property) would represent foregone revenue of $45.0 million in the year in which the equipment is purchased. Further, if the equipment had a four-year life before needing to be replaced, the foregone personal property tax revenue would total roughly $100.0 million over the four-year life cycle. Thus, exempting a $1.0 billion investment from sales/use and personal property taxes would be expected to result in about $36 million of foregone revenue on an annual basis.

Senate Bills 616 and 617 stipulate that the School Aid Fund (SAF) be held harmless from any sales or use tax revenue losses, so declines in sales and use tax revenue would only reduce Constitutional revenue sharing and General Fund/General Purpose (GF/GP) revenue. However, because the language requires the legislature to appropriate the necessary funds, there is no guarantee that the SAF will actually be held harmless since statute can't mandate an appropriation.

Reduced property tax collections will lower SAF revenue (via the 6-mill State Education Tax), local K-12 funding, revenue to local governments (cities, villages, townships, and counties), and other taxing authorities (libraries, community colleges, dedicated police and fire millages, etc.)

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