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ACCELERATE PHASE-IN
OF SALES AND USE TAX ON THE DIFFERENCE

Senate Bill 94 (reported from House committee w/o amendment)
Sponsor: Sen. Dave Hildenbrand

(Enacted as Public Act 2 of 2018)

Senate Bill 95 (reported from House committee w/o amendment)
Sponsor: Sen. Dave Robertson

(Enacted as Public Act 1 of 2018)

House Committee: Tax Policy
Senate Committee: Finance
Complete to 6-16-17

BRIEF SUMMARY: Senate Bill 94 would amend the General Sales Tax Act (MCL 205.51) to accelerate the phase-in of the dollar amounts that may be excluded from sales tax when a motor vehicle is used as a trade-in for a new or used motor vehicle. The limit on the amount that can be used as a trade-in would increase **$1,000 per year** instead of the current **$500 per year**, beginning in 2019.

Additionally, the bill would fully exempt from sales tax the agreed-upon value of a **recreational vehicle** when used as part payment of the purchase of a recreational vehicle purchased from a dealer.

Senate Bill 95 would amend the companion Use Tax Act (MCL 205.92) to make identical changes.

FISCAL IMPACT: Relative to current law, accelerating the phase-in of the exemption would reduce sales and/or use tax revenue by roughly $2.1 million in FY 2018–19, $5.1 million in FY 2019–20, and $7.5 million in FY 2020–21. The actual distributional impact of the revenue reduction depends on whether the loss is due to sales tax versus use tax revenue, although the most significant portion would likely be sales tax revenue. Approximately 72.8% of sales tax revenue is earmarked to the School Aid Fund, 10% to Constitutional revenue sharing, and 4.65% to the Comprehensive Transportation Fund. The remaining revenue accrues to the General Fund.

The revenue reduction will continue to increase by about $3 million per year through FY 2028–29, at which point the exemption would be fully phased in for an entire fiscal year. Between FY 2029–30 and FY 2038–39 (when the exemption would be fully phased in for an entire fiscal year under current law), the annual revenue reduction will grow smaller, and by FY 2038–39 the fiscal impact between current law and the accelerated phase in of the exemption would fall to zero. Relative to current law, accelerating the phase in of the exemption could result in reduced sales and/or use tax collections of at least $300 million.

THE APPARENT PROBLEM:

According to the bill's supporters, the "sales tax on the difference" legislation passed in 2013 (see **Background Information**) was a step in the right direction, but is not enough. With $500 annual increases to the maximum amount that can be excluded from sales tax, it will take over 20 years for the law to reach its full intended impact. This is too long to wait for Michigan residents to see what they describe as common sense tax relief. Advocates say that while the state took a step forward in 2013, it must continue to do more in order to make vehicle purchases more affordable for residents.

THE CONTENT OF THE BILL:

The bills would accelerate the phase-in and create the following schedule for the maximum value of a **motor vehicle** used as part payment.

Year	Maximum Trade-In Value
Jan 1, 2018 through Dec 31, 2018	$4,000
Jan 1, 2019	$5,000
Jan 1, 2020	$6,000
…	…
Jan 1, 2028	$14,000
Jan 1, 2029	No limit

As mentioned above, beginning January 1, 2018, there would be no limit on the value of a recreational vehicle when used as part payment of the purchase price of a recreation vehicle purchased from a dealer.

HOUSE COMMITTEE ACTION:

The Senate-passed versions of the bills were reported without amendment. An amendment was offered in committee to SB 95 that would have instituted a mechanism to hold the School Aid Fund harmless from revenue lost as a result of the bills. The amendment was not adopted.

BACKGROUND INFORMATION:

Public Act 160 of 2013 provided for an exemption from the sales tax, subject to a statutory limit, based on the agreed-upon value of a traded-in motor vehicle or RV when the trade-in is used as part purchase of a new or used motor vehicle or RV from a dealership (PA 234 made complementary changes in the Use Tax Act). This is commonly referred to as "sales tax on the difference."

With passage of the bills in 2013, purchasers who used a trade-in as part purchase of a new or used vehicle from a dealership paid sales tax on the "difference" between the sales price of the new or used vehicle and either, (1) the actual value of the trade-in vehicle, **or** (2) a specific dollar amount limit set in statute, whichever was less.

PA 160 set the initial limit on the value of the trade-in at $2,000 and provided for a "phase-in" period that gradually increased the maximum limit through $500 annual increases. The limit in calendar year 2017 is $3,500; meaning that even if the trade-in car is valued at $5,000, only $3,500 is exempt from sales tax. Under current law, by calendar year 2039, there would be no limit on the agreed-upon value of the trade-in.

ARGUMENTS:

Supporters of the legislation say:

- Twenty years is far too long to wait for real, tangible tax relief for Michigan residents. While the original phase-in schedule was negotiated during tight budget times, the state has more recently enjoyed increased revenues, and now is the time to accelerate the phase-in and provide tax relief. Allowing people to exempt more of their trade-in from sales tax is a common sense policy; in fact, some states charge no sales tax on vehicles!
- The entire automobile industry, from dealerships to manufacturers, could see increased revenue, jobs, and growth from this legislation. The accelerated phase-in will create an incentive for people to purchase new and used vehicles, which will benefit the overall state economy. Additionally, this is an easy tax cut to administer—it does not require any additional paperwork, processing, or time.

Opponents of the legislation say:

- The 2013 legislation was carefully crafted and negotiated to provide some form of tax relief while allowing schools and other entities to slowly absorb the lost revenues. Accelerating the phase-in breaks this agreement, without which no sales tax reduction would have been entertained. Why do we need to fix a tax policy issue that has already been fixed?
- The bills represent a continued erosion of the tax base that supports vital functions like schools and local governments. While one further exemption seems like a small change, the larger picture is the frequent introduction of legislation that provides special tax "carve outs" for specific items or businesses. In fact, these bills increase sales tax exemptions for what is most likely the largest purchase subject to sales tax for individuals. Since the bills directly impact sales tax revenue, the majority of revenue loss will be borne by the School Aid Fund.

POSITIONS:

A representative of the Auto Dealers of Michigan testified in support of the bills. (6-7-17)

Representatives of the following organizations indicated support of the bills:

- General Motors (6-7-17)
- Michigan Bankers Association (6-7-17)
- Michigan Boating Industries Association (6-7-17)
- Michigan Chamber of Commerce (6-7-17)
- National Federation of Independent Business (6-7-17, 6-14-17)
- Michigan Association of RVs and Campgrounds (6-7-17, 6-14-17)

Representatives of the following organizations testified in <u>opposition</u> to the bills:

- Michigan Department of Treasury (6-7-17)
- Michigan Association of School Boards (6-7-17)
- Michigan Education Association (6-7-17)

Representatives of the following organizations indicated <u>opposition</u> to the bills:

- Barry, Branch, Calhoun Jackson, Lenawee and Monroe ISD (6-7-17, 6-14-17)
- AFT Michigan (6-7-17, 6-14-17)
- Wayne RESA (6-7-17, 6-14-17)
- Michigan Association of Intermediate School Administrators (6-7-17, 6-14-17)
- Middle Cities Education Association (6-7-17, 6-14-17)
- Michigan Association of Secondary School Principals (6-7-17, 6-14-17)
- Michigan Association of School Administrators (6-7-17, 6-14-17)
- Oakland Schools (6-7-17, 6-14-17)
- Michigan Association of Counties (6-7-17)
- Michigan Townships Association (6-7-17)
- American Federation of State, County and Municipal Employees (6-14-17)

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