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BILL



ANALYSIS

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Senate Bill 887 (Substitute S-3 as reported)
Sponsor: Senator Jack Brandenburg
Committee: Finance

Date Completed: 3-29-18

RATIONALE

The General Sales Tax Act imposes a tax of 6% on the purchase price of tangible personal property in Michigan, and the Use Tax Act imposes a tax of 6% on tangible personal property that is used, stored, or consumed in Michigan, unless sales tax was paid when the property was purchased. Both Acts list property, transactions, and entities that are exempt from taxation. A concern has been raised about the taxation of personal property used in construction by a person who acquired the property from another, who purchased it. Currently, if a person consumes tangible personal property by affixing it to real property, the person is liable for the use tax levied on the property, regardless of whether the person purchased it. However, the liability can be satisfied if the person can demonstrate that another party paid sales or use tax on the property. This policy is believed to place an undue burden on construction contractors, particularly if a contractor cannot obtain sufficient proof from a customer that taxes were paid on the property. To alleviate this burden, it has been suggested that the State exempt from the use tax property that is used in constructing, altering, repairing, or improving real estate if the property was acquired by the contractor from the person who bought it.

CONTENT

The bill would amend the Use Tax Act to specify that the tax levied under the Act would not apply to tangible personal property acquired by a person engaged in the business of constructing, altering, repairing, or improving real estate for others to the extent that the property was purchased by another person that was not exempt from the tax levied under the Act or the General Sales Tax Act, and the property was provided to that contractor for the sole purpose of affixing that tangible personal property to and making it a structural part of real estate on behalf of the purchaser.

The bill states the following: "It is the intent of the legislature that this amendatory act clarifies that existing law as originally intended provides that the tax levied under this act does not apply to tangible personal property acquired by a person engaged in the business of installing tangible personal property if that tangible personal property is purchased by another for installation on behalf of that other person."

Proposed MCL 205.94ee

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 current practice of holding businesses and individuals liable for use taxes after using property provided by a customer for real estate construction purposes is unfair and illogical. If a person purchased light fixtures at a local home improvement store and hired a contractor to install them throughout the person's house, for example, the contractor should not be required to pay the use

tax on those light fixtures if he or she cannot provide sufficient proof that the customer paid taxes on the items.

According to Senate Finance Committee testimony, some Michigan businesses have been audited by the Michigan Department of Treasury and assessed use taxes that the businesses could be relieved of paying only if they could prove that taxes were paid on property provided to them by a customer for construction purposes. Examples of this situation include a business contracted by large retail stores, such as Target or Dick's Sporting Goods, to renovate a store or install equipment. These large retail stores typically are built to look similar, so it is not uncommon for a contractor to be given equipment, shelving, or other items for installation, instead of purchasing them on behalf of the store. In this case, the contracted business was audited by the Department and assessed \$558,000 in use taxes unless it could secure proof that taxes were paid on the materials provided to the contractor. While the business was eventually able to provide evidence to the Department, it was a burdensome task. Another company that installs equipment on cellular towers, however, has not been able to obtain proof that taxes were paid on certain cellular equipment it was contracted to install and may have to pay over \$90,000 in use taxes. Obtaining the confirmation requested by the Department is difficult, and sometimes may be impossible, since contractors do not have access to their customers' records. Furthermore, if the contractor is required to pay use taxes after not being able to secure proof that the customer already paid tax on the materials, the Department will be collecting taxes on the property twice.

It should be the Department's or the customer's responsibility to determine whether taxes have been paid on the property given to contractors. It is not fair to expect a contractor that was not a party to the purchase of the property to collect that information from the customer. Moreover, asking a customer for proof that taxes were paid on property could create friction between the customer and the contractor, and the customer could decide to take his or her business elsewhere. The current law places unfair expectations on contractors, and detracts from Michigan's inclusive business environment.

Michigan businesses should be focused on creating jobs and making money, not on proving who paid taxes on property provided to them. The bill would alleviate businesses of this responsibility and create fair and sensible policy.

Opposing Argument

The bill's provisions are unfair because they would create an exception for a specific type of transaction. In addition, the bill is ambiguous as to whether the responsibility to provide evidence that taxes were paid on property provided to a contractor would be transferred to the contractor's customer. Without clearer language, the bill could create a new issue of determining who would be liable for the payment of taxes in those situations.

Legislative Analyst: Drew Krogulecki

FISCAL IMPACT

The bill would have little to no impact on use tax revenue. The bill could possibly reduce revenue by an unknown amount in the case of a taxable purchaser acquiring property under tax-exempt provisions, and then transferring it to another person to affix to and make part of real property. Such circumstances would represent instances in which property was acquired for exempt purposes but later used for nonexempt purposes. An example would be where a purchaser acquired property for resale (an exempt purpose), but instead of being resold, the property was transferred to a person to affix it to real estate (a nonexempt purpose). Such situations are expected to represent a minimal number of use tax transactions, and thus would result in a minimal reduction to use tax revenue.

Fiscal Analyst: David Zin

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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.