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LESSOR TAX ELECTION

House Bill 4507 (Substitute H-1)
First Analysis (5-24-01)

Sponsor: Rep. Larry DeVuyst
Committee: Tax Policy

THE APPARENT PROBLEM:

The General Sales Tax Act and the Use Tax Act, taken together, allow a person or business entity engaged in the business of renting out or leasing tangible personal property the option of paying the sales tax on the property at the time of its purchase or paying the use tax on rental receipts. The issue of when and how this election is to be made to the Department of Treasury has reportedly been a vexing one for some time. According to testimony before the House Tax Policy Committee, in one recent case a businessperson in Michigan acquired a plane out of state to be leased for commercial use within the state. (This was said to be a first-time venture.) For a variety of reasons, however, including meeting federal licensing requirements, there was a delay in putting the plane into service and in notifying the state of the intent to pay tax on the lease receipts. The owner apparently should have notified state tax officials (and obtained a use tax registration) prior to the purchase, and the treasury department said the owner was obligated as a result to pay the tax on the purchase price of the plane. Legislation has been introduced to address this area of the tax law.

THE CONTENT OF THE BILL:

The bill would amend the Use Tax Act to specify the procedures to be followed if a lessor (a person or entity that conveys property by lease) elects to pay use tax on receipts from the rental or lease of tangible personal property in lieu of paying the sales or use tax on the full cost of the property at the time of its acquisition.

For tax years beginning after December 31, 1999, for property other than an aircraft, a lessor that elected to pay tax on receipts from the lease or rental of property would have to obtain a use tax registration before acquiring the tangible personal property.

If the property was an aircraft, for tax years beginning after December 31, 1999 and before January 1, 2002, a lessor that elected to pay tax on receipts from the lease or rental of the property would

have to obtain a use tax registration within 90 days after the lessor first brought the aircraft into the state.

If the property was an aircraft, for tax years beginning after December 31, 2001, the lessor would have to obtain a use tax registration by the earlier of 1) the date set for the first payment of use tax under the lease or rental agreement or 2) 90 days after first bringing the aircraft into the state.

The Department of Treasury would be required to provide a taxpayer, within 30 days after the taxpayer had obtained a use tax registration, with a written notice advising the taxpayer of the right to make an election under the bill's provisions and of the requirements to make a valid election.

MCL 205.95

BACKGROUND INFORMATION:

Rule 205.132 of the General and Specific Sales and Use Tax Rules currently says: "A person engaged in the business of renting or leasing tangible personal property to others shall pay the Michigan sales or use tax at the time he purchases tangible personal property, or he may report and pay use tax on the rental receipts from the rental thereof. A person remitting tax on the purchase price as a purchaser-consumer or remitting tax on rental receipts as a lessor, shall follow one or the other methods of remitting for his entire business operation. A person remitting tax on rental receipts shall be the holder of a sales tax license, or a registration as is provided in the Use Tax Act."

The definition of "sale at retail" in the General Sales Tax Act (at MCL 205.51) exempts sales of tangible property to persons for the purpose of resale or for lease, if the rental receipts are taxable under the Use Tax Act . . . The definition of "price" in the Use Tax Act (at MCL 205.92) contains the provision that the use tax shall not be computed or collected on rental receipts if the tangible personal property rented or

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leased has previously been subjected to a sales or use tax when purchased by the lessor.

FISCAL IMPLICATIONS:

The House Fiscal Agency reports that the fiscal impact of the bill is currently under review. (Fiscal Note dated 5-22-01)

ARGUMENTS:

For:

The bill provides some clarification regarding when a decision needs to be made regarding whether a lessor will pay sales or use tax at the time of purchasing tangible personal property or instead pay the use tax on the receipts from renting or leasing the property. Proponents say the Department of Treasury has admitted that this has been a problem area. Except in the case of aircraft, a purchaser of property would have to obtain the necessary use tax registration before acquiring the property that it intends to lease. However, the bill allows a purchaser of an aircraft 90 days after bringing the aircraft into the state (or the date set for the first payment of use tax, whichever was earlier) to obtain the necessary registration. It also would apply the 90-day aircraft provision retroactively to address at least one case in which the purchaser of an aircraft fell afoul of the current law. For those who do not regularly engage in this kind of transaction, it is a confusing process. Tax specialists say aircraft are a special case because of the various federal requirements that must be met before putting a plane in service. The bill, moreover, would make the Department of Treasury notify taxpayers about the requirements that must be followed in making the election between paying taxes on lease receipts or on the purchase price.

Against:

The Department of Treasury has supported creating a new special use tax provision for aircraft to be applied to future transactions, but opposes applying it to past cases (and presumably paying refunds). The department also has objections to the provision in the bill that requires the department to notify taxpayers of their ability to elect how to pay taxes, on the grounds that it may not accomplish its intended purpose.

POSITIONS:

The Department of Treasury has testified that it supports the provision that allows the tax election to take place 90 days after an aircraft has been brought

into the state, but opposes making the bill retroactive. The department also has concerns about the notification provision. (5-23-01)

A representative of Aero Genesis Aviation has indicated support for the bill. (5-23-01)

Analyst: C. Couch

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.