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SFA

BILL ANALYSIS

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Senate Bill 1422 (as enrolled)
Sponsor: Senator Joanne G. Emmons
Senate Committee: Finance
House Committee: Tax Policy

PUBLIC ACT 606 of 2002

Date Completed: 4-24-03

CONTENT

The bill amends the Single Business Tax (SBT) Act to exclude certain proceeds and other amounts from a taxpayer's gross receipts (which must be calculated to determine a taxpayer's SBT liability). The bill will take effect October 1, 2003.

The bill excludes from gross receipts the following: proceeds from the original issue of stock, equity instruments, or debt instruments; refunds from returned merchandise; cash and in-kind discounts; trade discounts; Federal, State, or local tax refunds; security deposits; payment of the principal portion of loans; value of property received in a like-kind exchange; proceeds from a sale, transaction, exchange, involuntary conversion, or other disposition of tangible, intangible, or real property that is a capital asset as defined in the Federal Internal Revenue Code or land that qualifies as property used in trade or business as defined in the Internal Revenue Code, less any gain from the disposition to the extent that gain is included in Federal taxable income; and the proceeds from an insurance policy, a settlement of a claim, or a judgment in a civil action, less any proceeds that are included in Federal taxable income.

The bill also excludes from gross receipts proceeds from the taxpayer's transfer of an account receivable, if the sale that generated the account receivable was included in gross receipts for Federal income tax purposes. This provision will not apply to a taxpayer that both buys and sells any receivables during the tax year.

(Under the Act, "gross receipts" means the entire amount a taxpayer received from any activity in intrastate, interstate, or foreign commerce carried on for direct or indirect benefit to the taxpayer or to others, except for

amounts specified in the Act. If a taxpayer's adjusted tax base exceeds 50% of the sum of the taxpayer's gross receipts plus certain adjustments, the taxpayer may reduce its adjusted tax base by that excess. Also, a taxpayer does not have to file an SBT return if its gross receipts, apportioned or allocated as provided in the Act, are under \$250,000.)

MCL 208.7

Legislative Analyst: George Towne

FISCAL IMPACT

The bill will reduce SBT revenues, and thus General Fund revenues, by an unknown and possibly significant amount. No information is available on the amount of accounts receivable that were sold but were generated by sales included in Federal taxable income of SBT filers, or on many of the other items the bill excludes from the definition of gross receipts. Some of the items the bill excludes have not historically been included in the definition of gross receipts and their presence in the bill makes technical clarifications in light of recent changes to that definition. For those items, such as trade discounts, tax refunds, security deposits, etc., the changes will have no fiscal impact. However, two exclusions in the bill will reduce revenues: 1) receivables sold, and 2) net proceeds from sales of certain capital assets.

In 1999, U.S. corporations reported \$7.7 trillion in notes and accounts receivable, compared with cash assets at year-end of \$1.6 trillion, \$1.4 trillion in holdings of U.S. government obligations, \$957 billion in tax-exempt securities, \$15.8 trillion in "other investments", \$2.6 trillion in "other current assets", and \$2.1 trillion in "other assets". The bill potentially will affect approximately

\$5.4 billion of accounts receivable assuming that: 1) Michigan activity represents approximately 3.5% of the U.S. total, and 2) the overwhelming majority (97%) of these accounts receivable are not sold to a third party. (The allowance for bad debts in 1999 totaled \$139.6 billion, or approximately 1.8% of notes and accounts receivable.) The bill restricts the exclusion to taxpayers that do not both buy and sell receivables. The share of the accounts receivable sold by taxpayers that both buy and sell receivables is unknown.

In 1999, if all taxpayers had filed using a computational method that included gross receipts, the provision excluding the sale of accounts receivable would have reduced SBT revenues by \$250.1 million, or approximately 10.6% of total SBT revenues. However, most SBT filers do not determine their tax with a computation that involves gross receipts, with approximately 11.9% of SBT filers in 1999 calculating their tax liability using a method affected by gross receipts. Assuming that accounts receivable affected by the bill are spread uniformly across all taxpayers regardless of how they calculate their SBT liability, approximately \$967.7 million in gross receipts actually would be affected by the bill. Excluding this amount from the gross receipts calculation would reduce revenues by approximately \$8.2 million, assuming the same differential between the number of filers using the gross receipts method and the impact on revenues. The estimate is very sensitive to the share of accounts receivable sold to third parties and there are no reliable data regarding that share. For example, if the share of accounts receivable sold to third parties were 2%, instead of the 3% previously assumed, the bill would reduce revenues by \$5.5 million.

The exception for taxpayers that both buy and sell receivables could reduce the impact from excluding sales of receivables from gross receipts by an unknown amount that likely depends on how the restriction is interpreted. Similarly, depending on how the restriction is interpreted, ensuring compliance with the tax law might be difficult, thus increasing the likelihood that the impact from that provision will not be reduced substantially.

The impact of exempting net proceeds from the sale of investments in real, tangible personal and intangible personal property is difficult to estimate because no information is

available regarding such sales or the share of assets affecting by these sales. If businesses sell 1% of their assets (mortgage and real estate loans, land, depreciable assets, depletable assets, and intangible assets, other investments, other current assets, other assets) that could be classified as investments in tangible, intangible or real property meeting the definitions in the bill, these provisions of the bill may reduce revenues by an additional \$8.1 million to \$9.1 million. As with the accounts receivable estimate, the estimate is very sensitive to the assumption. If 2% of the assets meet the criteria and are sold, rather than 1%, the fiscal impact increases to \$16.2 million to \$18.1 million.

When all the provisions are combined, the bill may reduce revenues by at least \$16.3 million, based on 1999 asset values.

The actual impact of excluding additional amounts from gross receipts might be slightly greater than the amount estimated above for the following reasons: 1) lowering gross receipts for firms will allow more firms to qualify for small business credits and/or file under the income tax method, 2) lowering gross receipts will increase the number of taxpayers that find it advantageous to file using a gross receipts method, 3) lowering gross receipts will mean that some taxpayers that otherwise might have liability will not be required to file a return. All of the bill's provisions might have greater impacts because the data above reflect information on corporations only, while the SBT taxes a broader array of businesses, including sole proprietorships, partnerships, S-corporations, and other firms not required to report information on the U.S. corporate income tax return.

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