



Senate Fiscal Agency
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Senate Bill 198 (as enacted)
House Bill 4404 (as enacted)
Sponsor: Senator Michelle A. McManus (S.B. 198)
Representative Steven Lindberg (H.B. 4404)
Senate Committee: Finance
House Committee: Tax Policy

PUBLIC ACT 115 of 2010
PUBLIC ACT 116 of 2010

Date Completed: 8-11-10

RATIONALE

Since 1999, Michigan law has contained sales and use tax exemptions for property used in industrial processing. Over the years, the exemptions reportedly have been applied inconsistently to equipment used to unload logs at sawmills, based on whether the logs were moved directly from a truck to a sawmill or, instead, were unloaded, sorted into piles on the ground, and then taken to the mill. The tax exemptions generally do not cover property that is used for receiving and storing materials or natural resources. Therefore, the equipment used to sort logs into piles, where they are considered stored, evidently has not been exempt, or has been taxed for the portion of time it was used for that purpose. The same tax treatment apparently has been applied to equipment used to move green lumber from a sawmill either directly to a truck or first to storage and then to a truck. Sawmill owners evidently have been assessed penalties as well as tax when they have purchased equipment, such as a front end loader, that was used at times for nonexempt purposes. To address this tax liability, it was suggested that the industrial processing exemptions be expanded.

Under the Use Tax Act, the tax does not apply property sold to an industrial processor for use in industrial processing; property sold to any person if the property is intended for ultimate use, and is used, in industrial processing by an industrial processor; property sold to a person who uses it to perform an industrial processing activity on behalf of an industrial processor; or a computer used in operating industrial processing equipment. Under the General Sales Tax Act, the tax does not apply to the sale of property under the same circumstances.

The Acts describe property that is eligible for the exemptions, including machinery, equipment, or materials used within a plant site or between plant sites operated by the same person for movement of tangible personal property in the process of production.

Under the bills, this exempt property includes front end loaders, forklifts, pettibone lifts, skidsters, multipurpose loaders, knuckle-boom log loaders, tractors, and log loaders used to unload logs from trucks at a sawmill site for the purpose of processing at the site and to load lumber onto trucks at a sawmill site for the purpose of transportation from the site.

The bills were tie-barred to each other and took effect on July 13, 2010.

MCL 205.94o (S.B. 198)
205.54t (H.B. 4404)

CONTENT

Senate Bill 198 amended the Use Tax Act and House Bill 4404 amended the General Sales Tax Act to extend the industrial processing exemptions to front end loaders and other specific types of equipment used at sawmills to unload logs and load lumber.

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 timber industry in Michigan has been struggling throughout the latest recession, as construction has declined and the demand for lumber has dropped. Although a slight improvement is beginning to be seen, some sawmill operations have gone out of business and others are barely surviving. An excessive financial burden resulting from the use and sales taxes could be the last straw, especially when penalties are assessed.

Sawmills rely on multiple types of equipment to unload, load, and move raw material around the facilities. Although some trucks are self-loading, sawmills often need to use other machinery, such as front end loaders, to unload logs, sort them by species, and move them from the piles to the mill. Depending on the equipment and what it is used for, it may or may not have been taxable. According to testimony on behalf of the Michigan Association of Timbermen, for example, a front end loader was considered taxable if it unloaded logs from a truck and placed them into different piles, but it was not taxable if it was used to take logs from either a pile or a truck and place them in the milling process. The same situation existed in regard to equipment used to move green lumber: The front end loader was exempt when it loaded a truck with lumber that came straight from the mill, but not if the lumber was placed in temporary storage before shipment, according to the Association. This tax liability could be significant, especially for a small operation. If a new loader cost \$200,000 and was used 50% of the time for nonexempt purposes, then \$100,000 was subject to the 6% use or sales tax, resulting in a tax of \$6,000 for one piece of equipment. Evidently, however, there was no standard formula for determining the percentage of time equipment was used for nonexempt purposes.

In 2008, legislation was enacted to address a similar problem with the taxation of equipment used in logging operations. Public Acts 555 and 556 of 2008 amended the Use Tax Act and the General Sales Tax Act, respectively, to exempt property sold to an extractive operator for transporting timber from the point of extraction to a place of temporary storage at the site and

loading or transporting timber from storage to a vehicle or other equipment that will remove it from the site. Senate Bill 198 and House Bill 4404 take the exemptions to the next stage in the process, when the logs arrive at a sawmill and are unloaded, sorted, and processed, and the green lumber is moved to trucks for shipment.

Response: Other types of facilities, such as veneer mills, pulp mills, and green energy producers, are involved in processing wood and also should receive an exemption for equipment used during the processing.

Opposing Argument

Both Acts state, "Industrial processing begins when tangible personal property begins movement from raw materials storage to begin industrial processing and ends when finished goods first come to rest in finished goods inventory storage." The expanded exemptions go beyond the boundaries of this definition, and set a precedent for exempting property used in activities that are not traditionally considered industrial processing. In addition, the only evidence of inconsistent tax treatment by auditors was anecdotal.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

Senate Bill 198

The bill will reduce use tax revenue by less than \$1.0 million annually. This loss in revenue will reduce the General Fund and the School Aid Fund, as two-thirds of use tax revenue is earmarked to the General Fund and the remaining one-third of the revenue is earmarked to the School Aid Fund. The bill will have no direct impact on local units of government.

House Bill 4404

Based on available information, the bill will lead to a reduction of approximately \$2.0 million in sales tax revenue. This reduction will primarily affect the School Aid Fund.

Given the reduction of sales tax revenue, there may be a reduction in revenue sharing payments to local government.

Fiscal Analyst: Eric Scorsone

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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.