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BILL ANALYSIS

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Senate Bill 201 (Substitute S-1 as passed by the Senate)
Sponsor: Senator Alan Sanborn
Committee: Finance

Date Completed: 7-7-09

RATIONALE

The General Sales Tax Act, as a rule, imposes a tax of 6% on the sales price of tangible personal property sold at retail. The sales price is the total amount of consideration, including cash, credit, property, and services, for which the property is sold. The sales price includes various costs and charges specified in the Act, as well as credit for any trade-in. This means that if a person purchases a new automobile, for example, and trades in a used one, he or she must pay sales tax on the full price of the new car. This strikes many people as unfair, because the sales tax originally was paid on the trade-in vehicle when it was purchased. A number of other states provide for a trade-in allowance when the sales tax is calculated on motor vehicle purchases, imposing the tax on the difference between the value of the trade-in and the price of the vehicle being purchased. It has been suggested that, in order to boost sales, Michigan should take the same approach, and extend it to other types of purchases, such as watercraft and heavy equipment, involving a trade-in.

CONTENT

The bill would amend the General Sales Tax Act to exclude from the sales tax the agreed-upon value of any of the following, if the agreed-upon value were separately stated on the invoice, bill of sale, or similar document given to the purchaser:

-- A titled watercraft used as partial payment of the purchase price of a new or used titled watercraft.
-- A motor vehicle or trailer coach used as partial payment of the purchase price of a new or used motor vehicle or trailer coach.
-- A piece of heavy earth-moving equipment used as partial payment of the purchase price of a new or used piece of heavy earth-moving equipment.
-- A titled snowmobile used as partial payment of the purchase price of a new or used snowmobile.

"New motor vehicle" would mean that term as defined in Section 33a of the Michigan Vehicle Code (a motor vehicle that is not and has not been a demonstrator, executive or manufacturer's vehicle, leased vehicle, or a used or second hand vehicle). "Heavy earth moving equipment" would mean industrial construction equipment that is self-propelled, weighs 10,000 pounds or more, and is designed and principally intended to move, transport, or reconfigure dirt, earth, soil, or other construction material at a construction site.

The Act's definition of "sales tax" would continue to include credit for any trade-in, *except* as described above.

MCL 205.51

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

Like the rest of the country, Michigan is and has been in a severe economic recession, although this State's heavy reliance on the motor vehicle manufacturing industry has contributed disproportionately to Michigan's financial woes. With Chrysler and General Motors having been forced to seek bankruptcy protection, and dealerships being closed, the State should do everything possible to boost auto sales. By allowing people to buy a new or used vehicle and avoid paying the sales tax on the value of a trade-in, the bill could give consumers the incentive they need to make a purchase. This point-of-sale tax break not only would help financially strapped individuals and families, but also would reduce the cost of doing business for companies that buy vehicles. At the same time, increasing sales would benefit dealers, suppliers, and other businesses—and their workers—that are affected by motor vehicle manufacturing and sales.

The bill also could boost sales of watercraft and snowmobiles by allowing a trade-in allowance for these items. In addition to giving purchasers a tax break and helping to sustain dealers, the bill could bolster the State's tourism industry.

Supporting Argument

Providing for sales tax on the difference in heavy earth-moving equipment transactions would benefit the construction industry, which also has been hard hit by the economic recession. A trade-in allowance would alleviate the overall tax burden on firms that must purchase extremely expensive pieces of equipment in order to perform their work and stay in business.

Opposing Argument

The State cannot afford to lose the sales tax revenue that is generated on vehicle sales, when billions of dollars must be cut from the budget and there is no evidence that the proposed tax break actually would spur sales. Auto companies already have tried a number of sales incentives, with little or no success. People are not buying cars because they are scared about losing their job, if they still have one, and cannot get a loan. It is unlikely that someone would be motivated to buy a $25,000 car just because he or she could save $600—or would choose not to buy the car without the tax break. The bill simply would give people a bonus for doing what they would do anyway, at an annual cost to the State of nearly $150 million.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bill would reduce sales tax revenue at least $145.0 million on a full fiscal year basis given the current depressed level of motor vehicle sales. This bill would reduce the sales tax liability when an automobile, light truck, motorcycle, watercraft snowmobile, heavy equipment, or motor coach is purchased when the transaction includes trading in a like vehicle. This loss in sales tax revenue would affect the following budget areas: School Aid Fund revenue would decline $106.3 million, Comprehensive Transportation Fund revenue would fall $6.7 million, and General Fund/General Purpose revenue would decline $7.8 million. In addition, revenue sharing payments to local governments would decline an estimated $24.2 million.

An example of how the provisions in this bill would change the sales tax liability on a new car purchase is as follows: Under current law, a person who purchases a new car for $25,000 and trades in a used car valued at $10,000 as part of the overall transaction, will have a sales tax liability equal to 6% of $25,000 or $1,500. Under this bill, the sales tax liability would be based on 6% of the difference between the price of the new vehicle ($25,000) and the value of the traded-in used vehicle ($10,000) or $15,000 times 6%, which equals $900. As a result, this bill would reduce the sales tax under this new car purchase example by $600 or 40%.

It is anticipated that the impact of this bill would not make any meaningful improvement in motor vehicle sales because the savings to consumers would not be significant enough given the current very weak motor vehicle market. Motor vehicle manufacturers and dealers are already offering price incentives on new motor vehicles averaging about $2,900 per vehicle to help bolster sales, but motor vehicle sales are still at historically low levels.

Some are claiming that the loss of revenue under this bill would not be as large as estimated because under the bill Michigan residents would no longer have an incentive to go to a neighboring state to purchase a motor vehicle in order to reduce their sales tax liability. However, the premise on which this argument is based – that Michigan residents can currently reduce their sales tax liability by purchasing a motor vehicle in another state – is not true. When a vehicle is purchased in another state and brought back to Michigan, the Michigan sales tax is assessed on that vehicle when it is registered in Michigan.

At the present time over 32 other states, including Illinois, Indiana, Ohio, and Wisconsin, provide some type of trade-in allowance when calculating the sales tax due on motor vehicle transactions.

Fiscal Analyst: Jay Wortley

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