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5136 Cascade Rd. SE #2A • Grand Rapids, MI 49546 • Phone: 616-575-3482 • Fax: 616-575-3481



[Ed Kisscorni, CPA/
MBA](#)

edk@ehtc.com

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Purchases from Other Firms: A Source of MBT Confusion

GRAND RAPIDS, MI – Monday, May 19, 2008 – At the Michigan Business Tax – Basic seminar last week in Pontiac, the most confusion and the greatest number of questions were about the subtraction for "purchases from other firms." The modified gross receipts tax consumed a lot of time. It should not be so surprising because of the newness of the tax to Michigan. However, the legislature has contributed to the confusion with their use of unfamiliar terms and their failure to adequately define terms. The Michigan Department of Treasury bears some of the blame for their attempts to ascertain legislative intent instead of reading the plain language of the law. This week we will review the three major components of "purchases from other firms."

Purchases from Other Firms

"Gross receipts" less exclusions is further reduced by "purchases from other firms" to arrive at the Modified Gross Receipts Tax Base. "Purchases from other firms" includes inventory, depreciable/amortizable assets and materials and supplies, including repair parts and fuel.

Inventory

(a) Inventory acquired during the tax year, including freight, shipping, delivery, or engineering charges included in the original contract price for that inventory.

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(4) "Inventory" means, except as provided in subdivision (d), all of the following:

(a) The stock of goods held for resale in the regular course of trade of a retail or wholesale business, including electricity or natural gas purchased for resale.

(b) Finished goods, goods in process, and raw materials of a manufacturing business purchased from another person.

(c) For a person that is a new motor vehicle dealer licensed under the Michigan vehicle code, 1949 PA 300, MCL 257.1 to 257.923, floor plan interest expenses for new motor vehicles. For purposes of this subdivision, "floor plan interest" means interest paid that finances any part of the person's purchase of new motor vehicle inventory from a manufacturer, distributor, or supplier. However, amounts attributable to any invoiced items used to provide more favorable floor plan assistance to a person subject to the tax imposed under this act than to a person not subject to this tax is considered interest paid by a manufacturer, distributor, or supplier.

(d) Inventory does not include either of the following:

(i) Personal property under lease or principally intended for lease rather than sale.

(ii) Property allowed a deduction or allowance for depreciation or depletion under the internal revenue code.

The deduction for "purchases from other firms" of "inventory" is limited to only retail, wholesale or manufacturing business.

Assets Acquired During the Tax Year

The taxpayer can subtract from gross receipts "purchases from other firms" of assets that are depreciable.

(b) Assets, including the costs of fabrication and installation, acquired during the tax year of a type

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that are, or under the internal revenue code will become, eligible for depreciation, amortization, or accelerated capital cost recovery for federal income tax purposes. [MCL 208.1113(6)(b)]

The deduction for the purchase of assets from other firms is based on the method of accounting used by the taxpayer for federal income tax purposes. The subtraction would be allowed in the taxable year that such costs are recorded in the taxpayer's books and records. This means construction in progress would be deducted in the year paid or accrued and recorded on the taxpayer's books and records.

The subtraction would not have to wait until the assets is placed in service and depreciated or amortized. Section 113(6)(b) includes the phrase "that are, or under the internal revenue code will become" which suggests the taxpayer does not have to wait until the assets is placed in service. The asset merely has to be "acquired during the year."

Materials and Supplies

The taxpayer can subtract from gross receipts "purchases from other firms" of "materials and supplies.

(c) To the extent not included in inventory or depreciable property, materials and supplies, including repair parts and fuel. [MCL 208.1113(6)(c)]

Treasury has stated in their FAQ M-4 that "materials and supplies" means tangible personal property acquired during the tax year to be used or consumed in and directly connected to the production or management of inventory under MCL 208.1113(6)(a) or the operation or maintenance of assets under MCL 208.1113(6)(b). "Materials and supplies" includes repair parts and fuel.

Treasury FAQ M-4 severely limits the deduction for materials and supplies whereas the statute does not. By limiting the deduction to the production or management of inventory and the operation and maintenance of assets; Treasury has blocked the deduction materials and supplies acquired by a contractor as well as any and all other purchases of materials and supplies by taxpayers.

Contractors are allowed a deduction for "payments to subcontractors for a construction project under a contract specific to that project."

Stay tuned for more news and follow the [MichiganStateAndLocalTaxBlog](#) for information as it becomes available.

If you have any questions, please go ahead and contact me. I would be happy to be of assistance.

Sincerely,

Ed Kisscorni, CPA/MBA



Echelbarger, Himebaugh, Tamm & Co., P.C.
5136 Cascade Rd. SE #2A
Grand Rapids, MI 49546

[\(616\)575-3482](tel:(616)575-3482) / ehc@ehc.com / www.ehc.com/

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