Senate Bill 748 (as introduced 1-11-18)
Sponsor: Senator Jack Brandenburg
Committee: Finance

Date Completed: 1-16-18

CONTENT

The bill would amend the Income Tax Act to do the following:

- Allow a personal exemption of $4,000 multiplied by the number of personal or dependent exemptions that would be allowable on a taxpayer's Federal return if the exemption amount under the Internal Revenue Code were greater than zero.
- Increase the personal exemption to $4,500 for the 2018 tax year, and increase the amount in $100 increments until it reached $4,800 for the 2021 and subsequent tax years.
- Revise the deduction for distributions from an ABLE savings account.

Personal Exemption

Part 1 of the Act imposes a tax at the rate of 4.25% on the taxable income of individuals. "Taxable income" means adjusted gross income as defined in the Internal Revenue Code (IRC), subject to a number of additions and deductions. In addition to these adjustments, the Act provides for a personal exemption multiplied by the number of personal or dependency exemptions allowable on the taxpayer's Federal income tax return under the IRC, to be subtracted in the calculation that determines taxable income. The bill would allow a personal exemption multiplied by the number of personal or dependent exemptions that would be allowable on the taxpayer's Federal income tax return "if the exemption amount pursuant to the internal revenue code was greater than zero".

Currently, the amount of the personal exemption is $4,000. The amount is scheduled to increase in $100 increments when an increase is triggered by inflation.

The bill would increase the personal exemption as follows:

- For the 2018 tax year, $4,500.
- For the 2019 tax year, $4,600.
- For the 2020 tax year, $4,700.
- For the 2021 tax year and each subsequent tax year, $4,800.

The bill would define "dependent" as an individual for whom the taxpayer may claim a dependent exemption on the taxpayer's Federal income tax return if the exemption amount was greater than zero under the IRC. The bill would repeal Section 30e of the Act, which defines "dependent" as an individual for whom the taxpayer may claim a dependent exemption on the taxpayer's Federal income tax return under the IRC.
Exempt Dependent

Under the Act, an individual with respect to whom a deduction under the IRC is allowable to another Federal taxpayer during the tax year is not considered to have an allowable Federal exemption for purposes of the Act's personal exemption calculation, and is exempt from the income tax and not required to file a return, if the person has an adjusted gross income of $1,500 or less. Under the bill, this would apply to a person with respect to whom a deduction under the Internal Revenue Code was allowable or would be allowable if the exemption amount were greater than zero.

ABLE Savings Account Distributions

Currently, to the extent not deducted in determining adjusted gross income, a taxpayer may deduct distributions that are qualified withdrawals from an ABLE savings account to the designated beneficiary of the account. Under the bill, a taxpayer could deduct these distributions to the extent included in adjusted gross income.

MCL 206.30 et al. Legislative Analyst: Drew Krogulecki

FISCAL IMPACT

The bill would reduce General Fund and School Aid Fund revenue from currently forecasted amounts by an unknown but significant amount in fiscal year (FY) 2017-18, depending on when the bill's changes became effective, by approximately $150.0 million per year from FY 2018-19 through FY 2020-21, and by a lesser amount that would decline each subsequent fiscal year--reaching zero by approximately FY 2026-27.

The reduction in revenue during FY 2017-18 would depend on when the bill was effective. If the changes for tax year 2018 were made retroactive, and effective beginning January 1, 2018, and income tax payments and withholding tables were adjusted to reflect that retroactivity, the bill would reduce FY 2017-18 General Fund and School Aid Fund revenue by approximately $110.9 million. If the bill's changes were not effective until April 1, 2018, revenue in FY 2017-18 would be reduced by approximately $73.9 million; however, the revenue reduction in FY 2018-19 would increase to approximately $184.4 million.

The impact of the bill would decline after FY 2020-21 because the difference between the value of the personal exemption under the bill and under current law would decline. Depending on the inflation rate over time, the difference would be expected to be eliminated by approximately FY 2026-27.

Under current law, approximately 23.8% of gross income tax revenue is earmarked to the School Aid Fund; therefore, that share of the total revenue reduction would lower School Aid Fund revenue. Consequently, if the bill lowered FY 2018-19 revenue by $147.4 million, School Aid Fund revenue would be reduced by $35.1 million, and the remaining $112.3 million in lower collections would reduce General Fund revenue.

In addition to the bill's impact relative to current revenue forecasts, the bill would reduce General Fund and School Aid Fund revenue relative to current law by approximately $1.1 billion in FY 2017-18, and approximately $1.4 billion in FY 2018-19. The revenue loss relative to current law would increase in subsequent fiscal years. These additional losses would reflect that the Federal tax reform legislation adopted in December 2017 would effectively eliminate the personal exemption under the Michigan individual income tax, thereby increasing revenue by approximately $1.1 billion in FY 2017-18 and $1.4 billion in FY 2018-19 (and additional amounts in future fiscal years). The bill's changes regarding the definition of "dependent" are
meant to effectively decouple Michigan’s current individual income tax provisions for dependents from the Federal tax reform changes. However, current revenue estimates do not account for the impact of Federal tax reform on Michigan's statutory tax provisions. Consequently, while the bill's changes to the definition of "dependent" would lower revenue relative to current law, the changes would not lower revenue relative to current revenue estimates.

While the changes to the definition would not lower revenue below current revenue estimates, the bill also would increase the personal exemption amount above the levels that would exist if the bill only decoupled Michigan tax provisions from the Federal tax reform legislation. As a result, the bill also would reduce revenue relative to currently forecasted levels.

Fiscal Analyst: David Zin