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BILL ANALYSIS

Senate Fiscal Agency

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Senate Bill 281 (as reported without amendment)  
Sponsor: Senator Doug Carl  
Committee: Finance

Date Completed: 4-18-89

**RATIONALE**

Public Act 516 of 1988, passed late last December, amended the Income Tax Act to require taxpayers to include lottery prizes as ordinary income, beginning with the 1988 tax year. Prior to the passage of Public Act 516, taxpayers were allowed to exempt lottery winnings from State and local taxes; winnings have always been subject to Federal income taxes. Some people argue, however, that the taxing of lottery prizes should not have been retroactive, that is, should not have applied to prizes that were won in 1988 or previous years. In fact, lawsuits reportedly have been filed against the State to challenge the ability of the State to tax lottery prizes awarded in 1988 or beyond but won in 1988 or previous years. It has been suggested that the tax on lottery prizes should apply only to prizes won after January 1, 1989.

**CONTENT**

The bill would amend the Income Tax Act to allow a deduction for money received by a taxpayer during the tax year as a result of a prize won before January 1, 1989, under the Lottery Act. This money could be deducted from taxable income to the extent that it was included in Federal adjusted gross income.

MCL 206.30

**FISCAL IMPACT**

The bill would lead to an indeterminate reduction in General Fund/General Purpose (GF/GP) revenue.

In FY 1987-88, of the \$587 million in total prize money, \$123 million represented installment payments for prizes won in prior years. Assuming all \$123 million would be included in taxable income, the bill would lead to a reduction in GF/GP revenue of approximately \$5 million to \$6 million per year. The reduction in GF/GP revenues would decline in future years as payments for prizes won prior to January 1989 expire.

**ARGUMENTS****Supporting Argument**

As a simple matter of fairness, the State should not tax the lottery winnings of persons who played lottery games and won prizes at a time when the State was prohibited from taxing lottery winnings. Passage of the retroactive tax on lottery winnings was not only unjust, it was an action that sent a harsh message to the residents of the State. The message was that the State runs the games and it makes the rules, and even if a person is fortunate enough to beat the tremendously low odds, the State can for its own convenience change the rules to diminish the amount winners thought they would be allowed to keep. The State should rescind the retroactive lottery tax before it is entangled in a mesh of legal challenges, and show the public that the State can forego some revenue for the sake of fairness.

**Opposing Argument**

The tax on lottery prizes was passed along with several other amendments that reduced income tax revenue. Public Act 516 also allowed low-income seniors, beginning in tax year 1989, to

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claim a credit for the cost of prescription drugs; in addition, it granted a \$500 deduction for dependents who earn over \$1,500 in 1988 and a \$1,000 deduction for 1989 and beyond. Applying the tax on lottery winnings to only those prizes won after 1988 would drastically reduce the revenues the State had expected to be generated from the tax. If the bill is passed, other sources of revenue should be found to counteract the effect of the bill.

#### Opposing Argument

The tax is retroactive only to the extent that it taxes prizes awarded in 1988 but won in previous years--it does not apply to prizes awarded before 1988. While the State has had a prohibition against the taxing of lottery winnings since the lottery's inception, it has been viewed by some as an unfair and unnecessary restriction on the State's ability to tax income. The levying of the 4.6% income tax on lottery winners cannot be viewed as a tax that causes a hardship on the taxpayers. A person who won \$1 million would, absent all deductions, be subject at the most to a tax bill of \$46,000 over the 20 years in which the prize was awarded.

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