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ESTIMATED TAX PAYMENTS: INCREASE THRESHOLD

House Bill 5453 as introduced
First Analysis (12-13-01)

Sponsor: Rep. Steve Vear
Committee: Tax Policy

THE APPARENT PROBLEM:

One of the recommendations of the October 2001 report of the Subcommittee on Tax Simplification of the House Tax Policy Committee is that the threshold at which taxpayers must begin making quarterly installment payments of taxes for state tax purposes be raised to the threshold for federal taxes. Currently under the state income tax, a taxpayer whose annual tax can reasonably be expected to exceed by $500 the amounts withheld and any credits allowed is required to make quarterly installment payments of estimated taxes. The federal threshold is, generally speaking, $1,000. The subcommittee report said: "Many taxpayers who are self-employed, buy or sell stock, or who have [or sell] a second home, owe the [state] over $500 in taxes at year end. These individuals may not actually realize that they are in this situation until their tax returns are prepared the following winter." This is particularly the case when the transaction is a one-time event like the sale of a home (resulting in taxable capital gains). It also affects taxpayers new to self-employment. Tax specialists say that if the payments are not made, taxpayers can be subject to penalties ranging from 10 percent to 25 percent of the amount owed. It would be easier to comply with this requirement if the state threshold was higher and was aligned with the federal threshold.

THE CONTENT OF THE BILL:

The bill would amend the Income Tax Act so that, for tax years beginning after December 31, 2001, the threshold for having to make installment payments would be the same as found in Section 6654(d) of the federal Internal Revenue Code. (At present this is, generally speaking, $1,000 or more in excess of amounts withheld and credits allowed.)

MCL 206.301

FISCAL IMPLICATIONS:

The House Fiscal Agency reports that bill would cause revenues to decrease by an indeterminate amount in that the Department of Treasury would lose interest on some quarterly estimated tax payments that it currently receives. (HFA fiscal note dated 12-10-01) The Department of Treasury reports that the bill would cost the state about $12.5 million in its first year of implementation in interest and penalties. In the next year, the revenue loss would be $4.5 million, with the amount to increase somewhat year by year. (Information provided by the Department of Treasury on 12-12-01)

ARGUMENTS:

For:

Supporters say that raising the state threshold for when quarterly installment payments of taxes are required, and aligning it with the federal threshold, will simplify the state tax laws in a manner helpful to taxpayers. This bill is based on a recommendation from the Tax Simplification Subcommittee of the House Tax Policy Committee. Testimony to that subcommittee from representatives of the Michigan Chapter of the National Association of Tax Practitioners contributed to that recommendation. Taxpayers now face stiff penalties if they do not make estimated payments when state taxes owed will exceed the amount already withheld by over $500. Taxpayers are sometimes unaware that they have accrued such a tax obligation, for example through the sale of a home or mutual funds. The federal requirement is set at the $1,000 level. Raising the state threshold to that amount will result in fewer errors by taxpayers and an element of consistency between state and federal tax laws.

Against:

It should be noted that the state tax rate is considerably lower than federal tax rates, and so it takes more income or gains to reach $1,000 in state taxes owed than in federal taxes owed. At a 4 percent tax rate, it takes $25,000 in additional income to produce an additional $1,000 state tax obligation. Federal tax rates run from 10 percent to over 30 percent. In that sense, the state and federal thresholds are not comparable. The bill also will have a revenue impact on the state. Treasury officials say the penalties and interest typically affect self-employed persons and sole proprietors.

POSITIONS:

The Department of Treasury is opposed to the bill. (12-12-01)

Analyst: C. Couch

■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.