

# Legislative Analysis

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## INCOME TAX DEDUCTION FOR EARLY DISTRIBUTION FROM IRA FOR MEDICAL EXPENSES

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**House Bill 5838**

**Sponsor: Rep. John Garfield**

**Committee: Tax Policy**

**Complete to 5-2-06**

### **A SUMMARY OF HOUSE BILL 5838 AS INTRODUCED 3-7-06**

The federal Internal Revenue Code imposes a 10 percent penalty on early distributions from qualified retirement plans, such as a 401(k) or IRA. (Generally, early distributions are those received before age 59 ½.) However, under Section 72(t)(2)(B) of the IRC, an taxpayer may receive an early distribution to pay unreimbursed medical expenses less than or equal the amount that may be deducted on an itemized federal return, without being subject to the 10 percent penalty. Section 213 of the IRC allows taxpayers to claim a deduction for unreimbursed medical expenses that exceed 7.5 percent of adjusted gross income. The taxpayer does not have to itemize in order to be exempted from the penalty provision. Early distributions are subject to taxation and are added with other types of income to determine federal adjusted gross income (AGI), which becomes the starting point on the Michigan income tax return.

House Bill 5838 would amend the Income Tax Act to permit taxpayers, in determining Michigan taxable income, to subtract from AGI early distributions made from an IRA for medical expenses—as described in IRC Section 72 (t)(2)(B)—to the extent that the distribution was included in determining AGI.

### **FISCAL IMPACT:**

The fiscal impact cannot be determined because the number of taxpayers that would qualify is not known. The resulting reduction in income tax revenue is likely to be relatively small.

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