Senate Fiscal Agency
P. O. Box 30036
Lansing, Michigan 48909-7536

BILL ANALYSIS

Telephone: (517) 373-5383
Fax: (517) 373-1986
TDD: (517) 373-0543

Senate Bill 640 (as enrolled) **PUBLIC ACT 513 of 2006**
Senate Bill 1393 (as enrolled) **PUBLIC ACT 512 of 2006**
House Bill 5022 (as enrolled) **PUBLIC ACT 514 of 2006**
Sponsor: Senator Buzz Thomas (S.B. 640)
Senator Bill Hardiman (S.B. 1393)
Representative David Robertson (H.B. 5022)
Senate Committee: Banking and Financial Institutions
House Committee: Banking and Financial Services

Date Completed: 1-17-07

RATIONALE

It was suggested that low-income people should have an opportunity to use the type of "individual development accounts" that are available to public assistance recipients under State and Federal law. The Personal Responsibility and Work Opportunity Reconciliation Act of 1996, sometimes called the national welfare reform act, authorizes states to create community-based individual development account (IDA) programs with Temporary Assistance for Needy Families (TANF) block grant funds. Individual development accounts are dedicated savings accounts that may be drawn upon to purchase a home, finance a postsecondary education, or start up a business. Accounts are managed by community organizations and held at local financial institutions. The community organizations, or "program sites" as they are known in IDA programs, also may offer personal financial management and home ownership classes. Money from public and private sources (such as TANF funds and grants from foundations) typically is used to provide a match to the savings of low-income participants in IDAs, providing an incentive for account holders to add to their savings.

In Michigan, Public Act 361 of 1998 amended the Social Welfare Act to require the Family Independence Agency, now called the Department of Human Services (DHS), to implement a program allowing an individual eligible for family independence assistance to establish an IDA for the purchase of a first home. Public Act 445 of 2004 amended the Social Welfare Act to allow IDA savings also to be used for postsecondary education and business capitalization.

Some people believe that use of IDAs to save for educational expenses, a first-time home purchase, or business capitalization should be available to low-income earners, as well as to those eligible for assistance. To that end, it was suggested that the law should extend that opportunity to anyone whose income is 200% of the Federal poverty level or less, and offer a tax credit to individuals who contribute to reserve funds that provide matching dollars to the deposits made by IDA holders. It was further suggested that the Social Welfare Act should treat the individual or family development account program similarly to the IDA program with regard to savings deposited into the accounts.

CONTENT

Senate Bill 640 created the "Individual or Family Development Account Program Act", and Senate Bill 1393 and House Bill 5022 amended the Social Welfare Act and the Income Tax Act, respectively, to do all of the following:

-- Establish the Individual or Family Development Account Program

within the Michigan State Housing Development Authority (MSHDA).

- -- **Require MSHDA to select program sites to administer the individual or family development accounts, and fiduciary organizations to provide technical assistance to program sites and establish and manage reserve accounts.**
- -- **Specify criteria for MSHDA to consider in reviewing the qualifications of program sites and fiduciary organizations.**
- -- **Allow an individual or family whose income is 200% of the Federal poverty level or less to establish a development account.**
- -- **Allow an account to be established only for the qualified expenses of paying for: 1) educational expenses of an account holder who is at least 17 years old; 2) the first-time purchase of a primary residence; or 3) start-up capitalization of a business for an account holder who is at least 18.**
- -- **Require a program site to enter into a participant savings plan agreement with each account holder, and provide matching funds for an account holder's contributions to the account.**
- -- **Require fiduciary organizations to file annual reports with MSHDA, and MSHDA to file an annual report with the Legislature.**
- -- **Require the DHS to operate the IDA program in coordination with the individual or family development account program operated by MSHDA under the Individual or Family Development Account Program Act.**
- -- **Allow a taxpayer who is not an account holder to claim a nonrefundable income tax credit equal to 75% of contributions made to a reserve fund under the Individual or Family Development Account Program Act.**
- -- **Specify that the income tax credits may not exceed an annual cumulative total of $1.0 million.**

The bills were tie-barred. Senate Bill 640 took effect on January 1, 2007. Senate Bill 1393 and House Bill 5022 took effect December 29, 2006.

<u>Senate Bill 640</u>

<u>Development Account Program</u>

The bill establishes the Individual or Family Development Account Program within MSHDA. The Program must provide eligible individuals and families with an opportunity to establish accounts to be used for education, first-time purchase of a primary residence, or business capitalization. The bill requires MSHDA to establish policies and procedures for the program, based on the policies and procedures adopted by the DHS to implement the Individual Development Account Program under Section 57k of the Social Welfare Act (MCL 400.57k).

The bill requires MSHDA to select both of the following:

- -- Program sites to administer the individual or family development accounts on a not-for-profit basis.
- -- Fiduciary organizations to provide technical assistance and support to program sites and establish and manage reserve accounts on a not-for-profit basis.

In reviewing the qualifications of fiduciary organizations and program sites, MSHDA must consider all of the following factors:

- -- The organization's not-for-profit status.
- -- The organization's fiscal accountability.
- -- The organization's ability to provide or raise money for matching contributions.
- -- The significance and quality of proposed auxiliary services to support the Program's goals.
- -- The availability of a financial literacy program for account holders.
- -- The ability to maintain and manage necessary program data for tracking account holders and participants in the Program and for development of reports required under the bill.

In reviewing the qualifications of fiduciary organizations, MSHDA also must consider an organization's ability to do all of the following:

- -- Administer one or more reserve funds to provide matching funds for account holders pursuant to participant savings plan agreements.

-- Administer any money appropriated by the State for the purposes of the Individual or Family Development Account Program Act.
-- Collaborate with program sites on a regional basis.
-- Provide technical assistance and support to program sites to assist them in administering programs effectively.
-- Work in conjunction with approved program sites to hold, manage, and disburse match funds for accounts as provided in the bill.
-- Maintain and manage necessary program data for tracking account holders and participants in the Program and for development reports required under the bill.

In reviewing the qualifications of program sites, MSHDA must consider the ability of a program site to develop and implement participant savings plan agreements to be used with account holders, that include at least all of the following:

-- The purpose for which the account is established.
-- The schedule of deposits that the account holder will make to the account.
-- The agreed-upon amount of matching funds and the projected date when the funds will be provided.
-- A plan to provide financial literacy; homeownership training; education, career, or business planning assistance, if appropriate; and any other services designed to increase the independence of the account holder, or his or her family, through the achievement of the designated purpose of the account.

Also, MSHDA must consider the ability of a program site to develop a partnership with all account holders with whom the program site has a participant savings plan agreement to assist them effectively to make financial decisions relating to the use of the funds available through the accounts, and to offer support services to maximize the opportunities provided by the Program.

The Authority must work cooperatively with financial institutions, fiduciary organizations, program sites, and contributors to implement the programs under the new Act, and may promulgate rules as needed to implement the Act.

Individual or Family Development Accounts

An individual or family whose household income is less than or equal to 200% of the Federal poverty level may apply to a program site to establish an individual or family development account. A program site may approve applications to the extent that it has match funds available to meet match commitments in participant savings plan agreements.

A program site may reject an application if approving it would result in the establishment of an account by one or more members of a family that has established an account for the same person for the same purpose. A household may not have more than one account for the same purpose if that purpose is a first-time purchase of a primary residence or start-up capitalization of a business.

If a program site approves an individual's or family's application to establish an account, the individual must do all of the following:

-- Establish the individual or family development account with a financial institution.
-- Enter into a participant savings plan agreement with the program site.
-- Declare, with the program site's approval, the purpose for which the account is established.
-- Meet any other criteria the program site requires.

An account may be established only to pay qualified expenses. An account may be established for one or more of the following purposes:

-- To pay educational expenses for the individual account holder who will be 17 or older when the funds in the account are used, if the account is for educational purposes.
-- For the first-time purchase of a primary residence by the individual account holder, if the account is for the purchase of a primary residence.
-- For start-up capitalization of a business for the individual account holder who is at least 18, if the account is for capitalization of a business based on a business plan approved by the program site.

For withdrawals, an account must require the signatures of the account holder and an administrator of the program site with which the account holder has a participant savings plan agreement.

"Educational expenses" means tuition and fees required for the enrollment or attendance of a student at an eligible educational institution, and expenses for fees, books, supplies, and equipment required for courses of instruction at an eligible educational institution. "Eligible educational institution" means a State university; a public community or junior college; an independent nonprofit college or university located in Michigan; a State-licensed vocational or technical education program; or a State-licensed proprietary school.

Participant Savings Plan Agreements

A program site must enter into a participant savings plan agreement with each account holder who is approved to establish an individual or family development account. The program site must provide matching funds for contributions to the account by the account holder pursuant to the agreement.

Matching fund distributions must be made on behalf of an account holder pursuant to a participant savings plan agreement at the same time that the account holder withdraws money to pay qualified expenses. Matching distributions must be at least a match of every $1 for every $1 withdrawn from an account by an account holder to pay qualified expenses or for a purpose approved by MSHDA. Matching distributions must be made by check to the order of the account holder and the entity he or she is paying.

Money withdrawn during a calendar year from an individual or family development account by an account holder for a qualified expense must be matched by the program site as provided in the participant savings plan agreement between the account holder and the program site.

Tax Credits

An individual who is not an account holder and who is subject to the State income tax may claim a credit under Section 272 of the Income Tax Act (which House Bill 5022 added), equal to 75% of contributions made to the reserve fund of a fiduciary organization. The total of all credits under Section 272 of the Income Tax Act may not exceed $1.0 million per calendar year.

The administrator of a fiduciary organization that administers one or more reserve funds, with the cooperation of the participating financial institutions, must submit to MSHDA the names of contributors and the total amount that each contributed to an individual or family development account reserve fund for each calendar year. The MSHDA director must determine the date by which the information is to be submitted.

A taxpayer who makes a contribution to a reserve fund must apply to MSHDA for certification that the contribution qualifies for a credit. An application must be approved or denied within 45 days after its receipt. If the application is not approved or denied within that time, it will be considered approved and MSHDA must issue a certificate stating that the taxpayer is eligible to claim a credit based on the contribution and the amount of the credit. If an application is denied, a taxpayer is not prohibited from subsequently applying for another contribution.

In reviewing tax credit applications, MSHDA must consider all of the following criteria:

-- The funds available to match contributions are deposited into a reserve fund in the same year that the credit is claimed.
-- The approval of the credit does not exceed the annual $1.0 million cap for all credits.
-- The overall benefit to the Program of the contribution for which a credit is requested.

A taxpayer may not claim a credit in excess of the amount approved by MSHDA. A taxpayer must attach the tax credit certificate received from MSHDA to the income tax return on which a credit is claimed.

Annual Reports

A fiduciary organization selected to administer an individual or family development account program must file with MSHDA an annual report of the organization's individual development account program activity. The report must be filed by September 30 each year, and include at least all of the following:

-- The number of individual development accounts administered by the fiduciary organization.
-- The amount of deposits and matching deposits for each account.
-- The purpose of each account.
-- The number of withdrawals made.
-- The number of terminated accounts and the reasons for termination.
-- Any other information MSHDA requires for the purpose of making a return-on-investment analysis.

By December 31 each year, MSHDA must file with the Secretary of the Senate and the Clerk of the House of Representatives a report that includes all of the information in the fiduciary organization reports described above and copies of any changes in policies or procedures used to administer the Act that occurred during the year.

Other Provisions

Contingent Beneficiary. An account holder must name at least one contingent beneficiary at the time the account is established and may change beneficiaries at any time. If an account holder dies, the account must be transferred to a contingent beneficiary. If the named beneficiary is deceased or otherwise cannot accept the transfer, the money must be transferred to the beneficiary's estate.

Withdrawal Verification. A financial institution is not responsible for verifying whether withdrawals from accounts held at the financial institution are made in accordance with and for a purpose allowed under the Act.

Senate Bill 1393

The Social Welfare Act requires the DHS to operate a program allowing an individual eligible for family independence assistance to establish an IDA for postsecondary education, business capitalization, or a first-time home purchase. The DHS must disregard all savings deposited in an IDA, including accrued interest, when determining an individual's eligibility for family independence assistance and the amount of the grant the individual receives. Under the bill, the DHS also must disregard all savings deposited, including accrued interest, in an individual or family development account.

The bill requires the DHS to operate the IDA program authorized under the Social Welfare Act in coordination with the Individual or Family Development Account Program operated by MSHDA under the Individual or Family Development Account Program Act.

House Bill 5022

Under the bill, for tax years beginning after December 31, 2006, a taxpayer who is not an account holder under the Individual or Family Development Account Program Act may claim an income tax credit equal to 75% of the contributions the taxpayer makes in the tax year to the reserve fund of a fiduciary organization pursuant to that Act.

If the amount of the income tax credit exceeds the taxpayer's tax liability for the tax year, the excess portion may not be refunded.

The credits under the bill may not exceed an annual cumulative maximum amount of $1.0 million. The determination of the maximum allowed must be made as provided in the Individual or Family Development Account Program Act.

MCL 206.701-206.711 (S.B. 640)
400.57k (S.B. 1393)
206.276 (H.B. 5022)

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

Individual or family development accounts are an innovative tool to help low-income earners save toward home ownership, educational advancement, or starting a small business. The provision of funds matching the amounts saved by the account holders will give eligible participants incentive to set aside some money. While the Social Welfare Act already included an IDA program for people receiving public assistance, Senate Bill 640 will help more people to save for the purchase of a first home, a college degree or vocational education, or small business capitalization. By implementing an individual or family development account program for low-income earners, regardless of whether they receive family independence assistance through the DHS, Senate Bill 640 extends to these individuals opportunities that may not otherwise be available to them.

Supporting Argument

The State's IDA program for assistance recipients has seen steady growth in open accounts and asset investment. According to written testimony provided to the Senate Banking and Financial Institutions Committee by the Michigan IDA Partnership, a joint operation of the DHS and the Council of Michigan Foundations, as of May 2006, there were five IDA program regional networks and 50 IDA program sites in Michigan. Since 2001, there have been more than 1,400 open/active account holders saving toward their IDA asset goal and, as of May 17, 2006, 796 IDA participants had made an asset investment. A woman from Jackson County testified before the Senate Committee that she saved $20 a month in an IDA for three years and in 2005 was able to use the savings and the matching funds for a down payment on a home purchase. She was hired as the coordinator for that IDA program site and told the Committee that one of her clients went from homelessness to home ownership in just two years. The success of this limited program suggests that a more widely available development program may greatly help Michigan's working families to save and invest in their futures, build financial security through ownership of assets, actively participate in the community, and contribute to the economy.

Supporting Argument

By granting a 75% income tax credit for contributions to a reserve fund, House Bill 5022 creates an incentive for taxpayers who do not hold an account to donate to a reserve fund that provides matching funds for account holders' deposits. The tax credit will encourage taxpayers to invest in Michigan's people and help to ensure that sufficient matching funds are available to supplement the savings of account holders, thereby increasing their opportunities to further their education, develop new business concepts, and invest in home ownership.

Response: Capping the total tax credit at $1.0 million limits the money available for reserve funds to match IDA savings. In addition, since one or a few taxpayers conceivably could contribute enough money to claim the entire amount of the available credit, the cap also may prevent some interested investors from receiving a tax benefit for their contributions.

Supporting Argument

The IDA program operated by the DHS requires that all savings deposited in an IDA, including accrued interest, be disregarded in the determination of an individual's eligibility for family independence assistance and the amount of the grant the individual receives. To maximize the effectiveness of the Individual or Family Development Account Program, Senate Bill 1393 requires that amounts deposited in and earned by an individual or family development account also be excluded from family independence assistance eligibility and grant determination criteria. In addition, by requiring that the DHS coordinate its program operation with MSHDA, the bill ensures that development account programs will be available both for assistance recipients and for other low-income earners on a similar basis.

Legislative Analyst: Patrick Affholter

FISCAL IMPACT

The Michigan State Housing Development Authority already administers similar programs, so the cost of the additional administrative responsibilities under the bills will be minimal.

The bills will have no fiscal impact on the Department of Human Services. Section 418 of Public Act 147 of 2005 and Public Act 345 of 2006 appropriates $200,000 in Federal Temporary Assistance for Needy Families funds "to expand the availability of individual development accounts...for allocation to qualified IDA programs...to serve TANF eligible households in Michigan".

The bills will reduce individual income tax revenue by a maximum of $1.0 million per year. It is unknown how many accounts will be created and how much will be saved, although during 2003, approximately 2.9 million individuals in Michigan, living in 675,000 families, resided in households with incomes of 200% of poverty or less. The amount that will be saved in the accounts is also unknown, and deposits to accounts will not receive any tax preferences or be subject to any specific maximums. Deposits to reserve funds will be eligible for a credit under the bills and also are likely to qualify for a deduction from Federal taxes. (Depending on the nature of the fiduciary organizations, the deposits also might be eligible for other credits under the Michigan tax structure.)

Because the bills specify a minimum matching contribution and the credit for deposits to reserve funds is limited to $1.0 million per year, under the assumption that reserve fund contributors will donate only to the level to which they will receive a tax credit, approximately $1.3 million per year will be deposited into reserve funds and be available to match a maximum of $1.3 million in savings by account holders annually. Deposits beyond this level may be made to the reserve funds, but will not be eligible for the tax credit.

A portion of the individual income tax impact is expected to reduce School Aid Fund revenue. The remaining impact will reduce General Fund revenue.

Several factors not addressed by the bills might influence participation: 1) The limited availability of matching contributions relative to the number of individuals who potentially qualify to open an account may reduce participation; 2) the income conditions for opening an account depend only upon income at the time the account is opened—once an individual (for example, while a student) opens an account, it will be available to him or her in perpetuity—even if the person's income (for example, after graduation) rises substantially above 200% of poverty, and this may serve to increase participation; 3) it is unclear how fiduciary organizations and financial institutions will cover the costs of participation in the program (particularly the costs of providing financial literacy education or financial independence services, or verifying that withdrawals are for eligible purposes), which may reduce participation or the availability of the program to the eligible population; 4) verification that individuals or families do not have multiple accounts will be handled at the program site level, allowing a limited number of individuals/families to gain accounts by using multiple fiduciary organizations and reducing the number of other eligible account holders who might participate in the program; and 5) there are no restrictions upon beneficiaries, so beneficiaries may include individuals who are not eligible to establish an account (for example, a lower-income elderly person establishing an account for a well-off child or grandchild) as well as entities that are not natural persons (such as a business or trust), which may increase participation. To the extent that low program participation affects the willingness of contributors to donate to reserve funds, the fiscal impact might be less than the $1.0 million if participation is low.

Fiscal Analyst: Constance Cole
Elizabeth Pratt
Maria Tyszkiewicz
David Zin