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BILL ANALYSIS

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Senate Bill 748 (as enacted) **PUBLIC ACT 314 of 2011**
House Bill 5157 (as enacted) **PUBLIC ACT 315 of 2011**
Sponsor: Senator Dave Hildenbrand (S.B. 748)
Representative Holly Hughes (H.B. 5157)
Senate Committee: Finance
House Committee: Tax Policy

Date Completed: 12-29-11

RATIONALE

The Michigan Renaissance Zone Act authorizes the State Administrative Board and the board of the Michigan Strategic Fund to designate a limited number of renaissance zones within local units of government, typically for a duration of up to 15 years. Renaissance zones are designed to promote economic development in blighted areas or support targeted industries by offering a variety of tax credits, deductions, and exemptions to individual residents of a zone and businesses that are located and conduct business activity in a zone. The Act cites specific sections of other statutes that permit these tax breaks, including Section 31 of the Income Tax Act, which essentially exempts individual residents of a renaissance zone from the State income tax. Section 31 is scheduled to be repealed on January 1, 2012, however, as a result of comprehensive changes to the individual income tax and business tax structures that were enacted in May 2011.

It was pointed out that eliminating the income tax exemption would have a negative impact on developers who have projects planned or under way in renaissance zones, and on the local units where the zones are located. Evidently, if residents could not be attracted by means of the tax exemption, some of these projects would not go forward or developers would be unable to recoup their investments. In turn, the local units would not experience the economic development benefits anticipated when the zones were designated. To avoid these consequences, it was suggested that the provisions of Section 31 should be re-enacted when the repeal takes effect, to retain the tax exemption with respect to existing renaissance zones.

CONTENT

Senate Bill 748 adds Section 31a to the Income Tax Act to allow a taxpayer to deduct income, dividends, capital gains, and lottery winnings, if the taxpayer is a resident of a renaissance zone for 183 consecutive days and his or her gross income does not exceed $1.0 million, and the renaissance zone was designated before January 1, 2012.

House Bill 5157 amended the Michigan Renaissance Zone Act to include a citation to Section 31a in a provision that lists the sections of law that allow an individual who is a resident of a renaissance zone, or a business that is located and conducts business activity in a renaissance zone, to receive an exemption, deduction, or credit.

The bills were tie-barred. Senate Bill 748 will take effect on January 1, 2012. House Bill 5157 took effect on December 27, 2011.

Below is a more detailed description of Senate Bill 748.

Under the bill, for the 2012 tax year and each subsequent tax year, and to the extent and for the duration provided in the Michigan Renaissance Zone Act, to determine taxable income, a qualified taxpayer may deduct, to the extent included in adjusted gross income, an amount equal to the sum of all of the following:

-- Except as provided in the following three items, income earned or received during the time the taxpayer was a resident of a qualified renaissance zone.
-- Interest and dividends received in the tax year during the period that the taxpayer was a resident of a qualified renaissance zone.
-- Capital gains received in the tax year prorated based on the percentage of time that the taxpayer held the asset while he or she was resident of a qualified renaissance zone.
-- Income the taxpayer received from winning a State-sponsored on-line or instant lottery game, if the drawing for the on-line game was held after the taxpayer became a qualified renaissance zone resident, or if the taxpayer was a qualified renaissance zone resident on the validation date of the ticket for the instant game.

If a qualified taxpayer completes the bill's residency requirements, he or she may claim the deduction. Within 10 days after completing the residency requirements, the taxpayer must file with his or her employer a withholding form prescribed by the Department of Treasury. A taxpayer also must file an annual return under the Income Tax Act to be eligible for the deduction.

If a taxpayer who was a qualified taxpayer during the tax year changes status and is not a qualified taxpayer, or vice versa, income subject to taxation must be determined separately for income in each status.

Income used to calculate a deduction under any other section of the Act may not be used to calculate a deduction under Section 31a. The net operating loss deduction allowed under the Act must be calculated without regard to the deduction allowed under Section 31a.

If the Department finds that a taxpayer has claimed a deduction under Section 31a to which he or she is not entitled, the taxpayer will be subject to the interest and penalty provisions of the revenue Act.

The bill defines "resident" as an individual domiciled in an area that is a qualified renaissance zone for 183 consecutive days. A taxpayer may begin calculating the 183-day period during the 183 days immediately before the designation of the area as a qualified renaissance zone. After completing the 183-day residency requirement, a taxpayer will be considered to have been a resident of that qualified renaissance zone from the first day used to determine if the requirement has been met. The term "resident" includes the estate of an individual who was a resident of a qualified renaissance zone at the time of death.

The bill defines "qualified renaissance zone" as only those geographic areas in a renaissance zone that was designated as a renaissance zone before January 1, 2012. A qualified renaissance zone does not include any portion of a renaissance zone for which an extension or renewal is approved after December 31, 2011.

"Qualified taxpayer" means a taxpayer who is a resident of a qualified renaissance zone and has gross income not exceeding $1.0 million for any tax year for which the taxpayer claims a credit under Section 31a.

MCL 206.31a (S.B. 748)
125.2689 (H.B. 5157)

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

In communities throughout the State, developers and others have made significant investments in renaissance zones, with the understanding that the income tax exemption would attract residents to the zones. Not all of the projects are complete, however, and the loss of the credit could have brought some developments to a standstill, essentially halting the turnaround that some cities or neighborhoods are experiencing. In downtown Muskegon, for example, after the mall was torn down and the property remained vacant for approximately 10 years, a renaissance zone designation has been instrumental in bringing the area back to life, with a new bank, shops, a culinary arts school, and townhouses. Another example involves the development of executive condominiums in a downtown Grand Rapids renaissance zone; because living in the city is more expensive than in the suburbs, these condos have been marketed with the promise of "Tax Free Living" until the zone's designation expires in 2017.

By creating renaissance zones and extending an income tax exemption to zone residents, the State made a commitment to communities, developers, investors, and individual residents that the tax break would be available for the duration of the zones' designation. This legislation upholds that commitment by retaining the exemption with respect to existing renaissance zones. As long as a zone was designated before January 1, 2012, individuals who meet the residency criteria can continue to enjoy the tax break until the zone's designation expires, and developers can complete their projects knowing that they will be able to attract residents.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

The bills will reduce State revenue by approximately $300,000 per year. Most of the reduction in revenue will affect the General Fund, with the remaining loss affecting the School Aid Fund. The School Aid Fund receives approximately 23.3% of income tax collections before credits, meaning that the maximum revenue reduction to the School Aid Fund will total approximately $70,000.

The bills will not affect local unit revenue or expenditures.

Fiscal Analyst: David Zin

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.