Legislative Analysis

PERSONAL EXEMPTION CHANGES

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Senate Bill 748 (substitute H-1)
Sponsor: Sen. Jack Brandenburg
House Committee: Tax Policy
Senate Committee: Finance
Complete to 2-14-18

(Enacted as Public Act 38 of 2018)

BRIEF SUMMARY:

Senate Bill 748 would amend the Income Tax Act to:

- Change definitions and references to reflect the recently enacted federal Tax Cut and Jobs Act of 2017 and remove reference to personal and dependency exemptions allowed on a taxpayer's federal income tax return.
- Allow a taxpayer to claim personal and dependency exemptions on the state income tax, and set the amount of the exemption in statute at $4,050 for the 2018 tax year, $4,400 for the 2019 tax year, $4,750 for the 2020 tax year, and $4,900 for the 2021 tax year, with a modified inflation adjustment returning thereafter.

[An exemption reduces the amount of income subject to tax.]

DETAILED SUMMARY:

Currently under the Income Tax Act, a taxpayer can claim a personal exemption and multiply the amount by the number of personal or dependency exemptions "allowable on the taxpayer's federal income tax return pursuant to the internal revenue code." The bill would remove the reference to the federal income tax return and provide for the determination of exemptions as follows:

- Each taxpayer may claim 1 personal exemption. If a joint return is not made by the taxpayer and his or her spouse, the taxpayer may claim a personal exemption for the spouse if the spouse does not have any gross income and is not the dependent of another taxpayer.
- A taxpayer may claim a dependency exemption for each individual who is a dependent of the taxpayer for the tax year.

With regard to the $1,500 deduction available to an individual to whom a deduction is allowable to another taxpayer, the bill would remove federal references and replace them with the exemption system described above.

Currently under the act, the personal exemption amount is set at either an inflation-adjusted amount (rounded to the nearest $100) or an amount specifically set in statute, whichever is greater. The personal exemption amount for tax year 2017 is $4,000.

The bill would set the following amounts in statute for the personal exemption:

- On and after January 1, 2014 and before January 1, 2018: $4,000.
- For the 2018 tax year: $4,050.
- For the 2019 tax year: $4,400.
- For the 2020 tax year: $4,750.
- For the 2021 tax year: $4,900.

For the 2022 tax year and each tax year thereafter, the inflation-adjusted amount would be increased by an additional $600.

The bill would repeal section 30e of the Income Tax Act. This section defines "dependent" as an individual for whom the taxpayer may claim a dependency exemption on the taxpayer's federal income tax return pursuant to the Internal Revenue Code.

The bill would add "dependent" to the definitions section of the act and define it as "a dependent as defined in section 152 of the internal revenue code."

The bill would change the definition of "internal revenue code" and define it as the United States Internal Revenue Code of 1986 in effect on January 1, 2018.

The bill would also repeal section 30f of the Income Tax Act, which provides for adjustments from taxable income for interest earned on the contributions to a taxpayer's education savings account and distributions that are qualified withdrawals from an education savings account, to the extent *not deducted* in determining adjusted gross income. Instead, the bill would allow a taxpayer to deduct, to the extent *included* in adjusted gross income, interest earned and qualified withdrawals.

The bill would make an identical change regarding interest and distributions for an ABLE savings account, allowing interest earned and qualified withdrawals to be deducted to the extent *included* in adjusted gross income.

MCL 206.8 et seq.

FISCAL IMPACT:

Under current law, the personal exemption is projected to increase due to inflationary adjustments from $4,000 in TY 2018 to $4,100 for TY 2019, $4,200 for TY 2020, and $4,300 for TY 2021. In contrast, Senate Bill 748 would increase the personal exemption to $4,050 in TY 2018, $4,400 in TY 2019, $4,750 in TY 2020, and $4,900 in TY 2021. In subsequent years, the personal exemption would equal the inflation-adjusted amount under current law plus $600. The table below presents the estimated personal exemption under current law, the proposed personal exemption under Senate Bill 748, and the estimated annual and cumulative revenue impacts.

Tax Year	Current Law Personal Exemption	Proposed Personal Exemption	Fiscal Year	Annual Impact (millions)	SAF Impact (millions)	GF/GP Impact (millions)	Cumulative Impact (millions)
2018	$4,000	$4,050	FY 2017-18	($7.5)	($1.8)	($5.7)	($7.5)
2019	$4,100	$4,400	FY 2018-19	($75.0)	($17.0)	($58.0)	($82.5)
2020	$4,200	$4,750	FY 2019-20	($146.3)	($34.8)	($111.4)	($228.8)
2021	$4,300	$4,900	FY 2020-21	($176.3)	($41.9)	($134.3)	($405.0)

In subsequent years, the $600 differential would reduce income tax revenue by about $180.0 million relative to current law, and would reduce revenue to the School Aid Fund by about $43.0 million per year. The remaining $137.0 million reduction would come from the general fund.

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