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

BILL ANALYSIS

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

Senate Bill 405 (Substitute S-1 as passed by the Senate)
Sponsor: Senator Tonya Schuitmaker
Committee: Finance

Date Completed: 1-8-18

RATIONALE

Legislation enacted in 2011 restructured business and personal income taxes by repealing the Michigan Business Tax (for most taxpayers) and replacing it with the new Corporate Income Tax; eliminating a number of personal income tax deductions, exemptions, and credits, including credits for charitable contributions; and making various other changes. Apparently, many charitable organizations have suffered since the restructuring due to reduced contributions. These organizations include the many food banks, shelters, and community foundations that are found in most Michigan communities. Some believe that reinstating tax credits for donations to these types of entities would provide the necessary incentive for individuals to give more to charitable organizations or other institutions that provide services to the public.

CONTENT

The bill would amend Part 1 of the Income Tax Act to do the following:

-- **Allow a taxpayer to claim a credit against the income tax equal to 50% of the aggregate amount of charitable contributions made to a shelter for homeless people, food kitchen, food bank, or similar entity; an accredited zoo; or a museum.**
-- **Allow a taxpayer to claim an additional credit for 50% of the amount contributed during the tax year to a community foundation.**
-- **Limit each credit to $100 for an individual or $200 for a joint return; or, for a resident estate or trust, 10% of tax liability before credits or $5,000, whichever was less.**

(Part 1 of the Act imposes a tax on the income of individuals and noncorporate entities.)

Specifically, for tax years beginning on and after January 1, 2018, the bill would allow a taxpayer to claim a credit for an amount equal to 50% of the aggregate amount of charitable contributions made by the taxpayer during the tax year to any of the following if a contribution to that entity were tax deductible for the donor under the Internal Revenue Code:

-- A shelter for homeless people, food kitchen, food bank, or other entity located in Michigan, whose primary purpose is to provide overnight accommodation, food, or meals to people who are indigent.
-- A zoological park accredited by the American Association of Zoos and Aquariums.
-- A museum.

The maximum allowed under this credit for total contributions made, including the value of food items contributed in conjunction with a program in which a vendor made a matching contribution of similar items in the tax year to shelters for homeless people, food kitchens, food banks, and, except for community foundations, other entities, would be as follows:

-- For a taxpayer other than a resident estate or trust, $100, or $200 for a joint return.

- For a resident estate or trust, 10% of the taxpayer's tax liability for the tax year before claiming any credits allowed by Part 1 of the Act or $5,000, whichever was less.

For tax years beginning on and after January 1, 2018, a taxpayer could claim an additional credit for an amount, subject to applicable limitations, equal to 50% of the amount contributed during the tax year to a community foundation. For a taxpayer other than a resident estate or trust, the credit for a contribution to a community foundation could not exceed $100, or $200 for a joint return. For a resident estate or trust, the credit could not exceed 10% of the taxpayer's liability for the tax year before claiming any credits allowed by Part 1 or $5,000, whichever was less. For a resident estate or trust, the amount used to calculate the proposed credit could not have been deducted in arriving at Federal taxable income.

If the amount of the credits allowed under the bill exceeded the tax liability of the taxpayer for the tax year, the excess portion could not be refunded.

An entity other than a community foundation could request that the Department of Treasury determine if a contribution to that entity qualified for the proposed credit. The Department would be required to make a determination and respond to a request within 30 days after it received the request.

A taxpayer could claim a credit under the bill for contributions to a community foundation made within an 18-month period after a community foundation was incorporated or established. During that 18-month period, the community foundation would have to build an endowment value of $100,000. If the community foundation did not reach the required endowment value during that period, contributions to the community foundation made after the date on which the 18-month period expired could not be used to calculate a credit under the bill. If the community foundation had an endowment value of $100,000 at any time after the 18-month period expired, the foundation could apply to the Department for certification.

By July 1 of each year, the Department would be required to report to the House Committee on Tax Policy and the Senate Finance Committee the total amount of tax credits claimed under the bill for the immediately preceding tax year.

"Community foundation" would mean an organization that applies for certification on or before May 15 of the tax year for which the taxpayer is claiming the credit, and that the Department certifies for that tax year as meeting all of the following requirements:

- Qualifies for exemption from Federal income taxation under Section 501(c)(3) of the Internal Revenue Code (which generally applies to nonprofit, charitable organizations).
- Supports a broad range of charitable activities within the specific geographic area of Michigan that it serves, such as a municipality or county.
- Maintains an ongoing program to attract new endowment funds by seeking gifts and bequests from a wide range of potential donors in the community or area served.
- Is publicly supported as defined by the regulations of the U.S. Department of Treasury, and annually submits to the Michigan Department of Treasury documentation demonstrating compliance with this requirement.
- Is not a supporting organization as described in Section 509(a)(3) of the Internal Revenue Code and U.S. Department of Treasury regulations (i.e., a charity that carries out its exempt purposes by supporting other exempt organizations, usually other public charities).
- Meets the requirements for treatment as a single entity contained in regulations of the U.S. Department of Treasury.
- Is incorporated or established as a trust at least six months before the beginning of the tax year for which the proposed credit is claimed and has an endowment value of at least $100,000 within 18 months after the community foundation is incorporated or established, except as provided in the bill.
- Has an independent governing body representing the general public's interest that is not appointed by a single outside entity.

-- Gives the Michigan Department of Treasury evidence that the community foundation has, within six months after it is created, and maintains continually during the tax year for which the proposed credit is claimed, at least one part-time or full-time employee.

Also, a community foundation having an endowment value of $1.0 million or more would be subject to an annual independent financial audit and would have to provide copies of that audit to the Department within three months after its completion. A community foundation with an endowment value of less than $1.0 million would be subject to an annual review and an audit every third year.

In addition to all other criteria listed in the bill, a community foundation that was incorporated or established after June 22, 2000, would have to operate in a Michigan county that was not served by a community foundation when the community foundation was incorporated or established or would have to operate as a geographic component of an existing certified community foundation.

"Museum" would mean an institution generally known as a museum or archive located in the State that meets each of the following:

-- Is established primarily for artistic, educational, scientific, historic, or preservation purposes.
-- Exhibits, cares for, studies, archives, or catalogs property.
-- Is operated by a nonprofit corporation, college, university, or public agency.

Proposed MCL 206.261

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

Charitable organizations, public institutions, and other nonprofit groups are critical to the provision of necessary services to individuals in Michigan, and usually rely on charitable donations. Often, those services involve assisting individuals or communities that need help, and can be essential during crises. It is important to encourage taxpayers to support nonprofits, charitable organizations, and public institutions and to give those entities the resources necessary to fulfill their missions.

The bill would support organizations that combat hunger problems in Michigan. According to the Michigan League for Public Policy, despite the economic recovery after the "Great Recession", approximately 1.5 million Michigan residents do not have enough to eat.

According to the Council of Michigan Foundations, every dollar the State gives in charitable tax credits returns three to charitable contributions. When nonprofits deliver critical services, the burden on the State is reduced. The bill would encourage people to contribute to worthy charities across Michigan, and display the State's commitment to supporting charitable giving.

Supporting Argument

Nonprofit organizations make significant and direct contributions to Michigan's economy. According to Michigan Nonprofit Association data, there are more than 47,000 nonprofits throughout Michigan, which employed more than 451,000 people in 2015 (almost 11% of the Michigan workforce). Nonprofits pay these employees over $4.9 billion per quarter while holding nearly $240.0 billion in assets, and spend more than $80.0 billion each year.

Because nonprofits rely on charitable donations for a majority of their funding, providing a tax credit incentive to taxpayers would encourage donations that enable types of the institutions listed in the bill to help many individuals throughout the State, and contribute to the Michigan economy as a whole.

Opposing Argument

In 2011, tax reform legislation was enacted to simplify the tax code and remove unnecessary complexity. That goal was accomplished and it remains good policy. In addition to departing from that policy, the bill would create inequality among charitable institutions, as the credit would be targeted toward a certain type of institution while others, such as those that volunteer time, would receive no benefit. There is nothing precluding taxpayers from contributing to charitable foundations or nonprofits.

Response: Although making charitable contributions can become a habit among taxpayers, the legislation that removed the tax credits seriously damaged the "pipeline" of charitable donations. This claim is supported by data from the Johnson Center at Grand Valley State University, which completed a survey on donations to Michigan community foundations. The survey examined changes in the number of $200 and $400 donations−the amount that would trigger the maximum credit before it was repealed. The data show an 84% decline in first-time donors at the $400 level from 2010 to 2013, and a 37.5% decline in first-time donors at the $200 level from 2010 to 2013. Additionally, the data show a 76% decline in $400 donations from 2011 to 2013, and a 44% decline in $200 donations from 2011 to 2013 as a whole.

Legislative Analyst: Drew Krogulecki

FISCAL IMPACT

The bill would reduce General Fund revenue by approximately $23.5 million per year. Between tax years 2006 and 2011, the number of returns claiming the credit for contributions to homeless shelters and food banks remained relative stable, at approximately 234,500 each year, as did the number of returns claiming the community foundation credit, at approximately 38,900. Similarly, the total amount claimed each year under each credit remained stable, at approximately $18.7 million for the homeless shelter/food bank credit and approximately $3.3 million for the community foundation credit. Credits for donations to cultural institutions such as museums and zoos reduced revenue by approximately $1.5 million per year. Although the School Aid Fund receives revenue from the income tax under Part 1 of the Act, credits are applied against the portion received by the General Fund. As a result, all of the reduction in revenue under the bill would lower General Fund revenue.

The actual revenue reduction from the bill could be greater than estimated based on the historical cost of the credits, because the bill would not reinstate a significant restriction on eligible contributions. When the credit for donations to food banks and homeless shelters existed before in Michigan statute, in order to qualify for the credit, donations from resident estates and trusts could not have been deducted in arriving at Federal taxable income. Because the bill would not reinstate this provision, resident estates and trusts would be able to claim the credit for contributions that also were used to reduce Federal taxable income, presumably increasing the number and amount of contributions that would be claimed under the credit.

Fiscal Analyst: David Zin

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