

Legislative Analysis



CREATE THE MICHIGAN FIRST-TIME HOME BUYER SAVINGS PROGRAM

Phone: (517) 373-8080
<http://www.house.mi.gov/hfa>

House Bill 4289 (H-2) as reported from committee
Sponsor: Rep. John N. Damoose

Analysis available at
<http://www.legislature.mi.gov>

House Bill 4290 as reported from committee
Sponsor: Rep. Mari Manoogian

Committee: Tax Policy
Complete to 4-9-21

BRIEF SUMMARY: Together, House Bills 4289 and 4290 would create the Michigan First-Time Home Buyer Savings Program. The program would allow individuals to create savings accounts with state income tax benefits for the purpose of using the funds for a down payment on a house.

FISCAL IMPACT: Determining the fiscal impact depends on the number of taxpayers who avail themselves of the program and the annual amount saved. (See **Fiscal Information**, below, for further discussion.)

THE APPARENT PROBLEM:

Homeownership is often seen as a key to the American Dream: it fosters community and civic engagement, leads to stability for youth in local schools, and promotes self-sufficiency. But for many, one challenge remains on the path to homeownership: the down payment. A down payment of 5% to 10% of the purchase price might now be seen as a ballpark estimate. While the exact mortgage terms and loan programs vary, saving around \$10,000 for the down payment on an average-priced \$140,000 home is difficult. Many believe that more can be done to support this type of saving. Legislation has been introduced to provide for savings accounts with state income tax benefits to be used for the down payment on a home in Michigan.

THE CONTENT OF THE BILLS:

House Bill 4289 would create a new act to establish the Michigan First-Time Home Buyer Savings Program (“program”) in the Department of Treasury (“Treasury”). The purposes, powers, and duties of the program would be vested in and exercised by the state treasurer or his or her designee.

Under the bill, beginning January 1, 2022, any individual could open an account with a *financial institution* and designate the account, in its entirety, as a *first-time home buyer savings account* to be used to pay or reimburse a *qualified beneficiary’s eligible costs* for the purchase of a *single-family residence* in Michigan.

Financial institution would mean any bank, trust company, savings institution, industrial loan association, consumer finance company, credit union, or any benefit

association, insurance company, safe deposit company, money market mutual fund, broker, or similar entity authorized to do business in Michigan.

First-time home buyer savings account (“account”) would mean an account with a financial institution that an account holder designates as a first-time home buyer savings account on his or her income tax return pursuant to the proposed act, for the purpose of paying or reimbursing eligible costs for the purchase of a single-family residence in Michigan by a qualified beneficiary.

Qualified beneficiary would mean a first-time home buyer who is designated as the beneficiary of an account designated by the account holder as a first-time home buyer savings account.

Eligible costs would mean the down payment and allowable closing costs for the purchase of a single-family residence in Michigan by a qualified beneficiary.

Single-family residence would mean a single-family residence owned and occupied by a qualified beneficiary as the qualified beneficiary’s principal residence, and would include a manufactured home, trailer, mobile home, condominium unit, or cooperative.

An ***account holder*** would have to designate a ***first-time home buyer*** as the qualified beneficiary for the account. The account holder could designate himself or herself as the qualified beneficiary, and could change the qualified beneficiary at any time, but there could not be more than one beneficiary at any one time.

Account holder would mean an individual who establishes, individually or jointly with one or more other individuals, an account with a financial institution for which the account holder claims a first-time home buyer savings account status on his or her Michigan income tax return.

First-time home buyer would mean an individual who is a Michigan resident and has not owned or purchased, individually or jointly, a single-family residence during a period of three years prior to the date of the purchase of a single-family residence.

An individual could jointly own an account with another person if the joint account holders file a joint return under the Michigan income tax act. An individual could be the account holder of more than one account, but could not have multiple accounts with the same qualified beneficiary. An individual could be the beneficiary on more than one account.

Only cash and marketable securities could be contributed to an account, and anyone could contribute. The maximum account balance would be capped at \$50,000, but an account that had reached the maximum balance could continue to accrue earnings. Contributions to and interest earned on an account would be exempt from taxation, as would ***qualified withdrawals***.

Qualified withdrawal would mean a withdrawal from an account that is not subject to a penalty under the proposed act or taxation under the Income Tax Act and that is either of the following: (1) a withdrawal from an account to pay the eligible costs of the qualified beneficiary incurred after the account is established, or (2) a withdrawal made as the result of the death or disability of the qualified beneficiary of an account.

If funds were withdrawn from an account for any purpose other than the payment of eligible costs by or on behalf of a beneficiary, a 10% penalty, payable to Treasury, would be assessed on the amount withdrawn. The penalty would not apply if the funds were withdrawn for any of the following reasons: (1) withdrawn by reason of the beneficiary's death or disability, (2) a disbursement of assets of the account pursuant to a filing for protection under chapter 11 of the United States Bankruptcy Code, (3) transferred from a home buyer savings account into another home buyer savings account, or (4) withdrawn because a qualified beneficiary who is a service member is transferred or deployed out of state on active duty.

The account holder would be responsible for the use or application of funds in the account. The account holder would not be able to use the funds in an account to pay expenses of administering the account, except that a service fee could be deducted from the account by the financial institution. An account holder could withdraw funds from an account and deposit the funds in a new account held by a different financial institution or the same financial institution.

An account holder would have to submit, with the account holder's state income tax return, all of the following to Treasury:

- Account statements that show the contributions during the tax year and the taxable interest or earnings on the account for the applicable tax year.
- The applicable Form 1099 issued by the financial institution for the account.
- Upon withdrawal of funds, a copy of the real estate settlement statement that shows that the withdrawal was used for eligible costs.

An account holder would need to maintain and keep, for at least four years, specified records for the account.

Treasury would have to prescribe the form and manner for claiming the deduction. The form would have to include at least the account holder's name, the name of the qualified beneficiary, the name of the financial institution, the account number, the beginning and ending account balance, and the amount of the deduction claimed.

The state treasurer could promulgate rules to implement the program. The rules could not impose any obligations or requirements on financial institutions-related accounts for first-time home buyer savings accounts. Treasury could also prepare and distribute informational materials on the savings program to financial institutions and potential home buyers.

The financial institution would not be required to do any of the following:

- Designate an account as a home buyer savings account, or designate the qualified beneficiaries of an account, in the institution's contracts or systems.
- Track the use of money withdrawn from an account.
- Allocate funds in an account among joint account holders or multiple beneficiaries.
- Report any information to Treasury that is not otherwise required by law.

A financial institution would not be liable for any of the following:

- Determining that an account satisfies the requirements to be a first-time home buyer savings account.
- Determining that the funds in an account are used for eligible costs.
- Reporting or remitting taxes or penalties related to the use of an account.

If provided with the proof of death of the account holder and any other information required of the savings account contract, a financial institutional would have to distribute the principal and accumulated interest in the account in accordance with the terms of the contract.

House Bill 4290 would amend Part 1 of the Income Tax Act to provide for the tax benefits of the accounts as follows:

For tax years that begin after December 31, 2021, a taxpayer could deduct all of the following:

- To the extent not deducted in determining adjusted gross income (AGI), contributions made by the taxpayer in the tax year less qualified withdrawals made in the tax year from a first-time home buyer savings account, not to exceed a total deduction of \$5,000 for a single return or \$10,000 for a joint return per tax year. The amount calculated would have to be greater than zero, and a deduction could not be claimed for more than 20 tax years.
- To the extent not deducted in determining AGI, interest earned in the tax year on the contributions to the account, if the contributions were deductible.
- To the extent included in AGI, distributions that are qualified withdrawals from an account to the beneficiary of the account.

The taxpayer would have to add, subject to certain limitations and to the extent not included in AGI, the amount of money withdrawn by the taxpayer in the tax year from the account, not to exceed the deduction of contributions less qualified withdrawals, if the withdrawal was not a qualified withdrawal.

MCL 206.30

The bills are tie-barred to each other, which means that neither could take effect unless both were enacted.

BACKGROUND INFORMATION:

The bills are reintroductions of Senate Bills 511 and 512 of the 2017-18 legislative session. Those bills were passed by the House and Senate but were vetoed by Governor Snyder on December 21, 2018. In his veto message, the governor indicated support for the goal but questioned the use of the tax code to incentivize taxpayer behavior.¹

FISCAL INFORMATION:

In 2019, first-time home buyers accounted for about 33% of all home purchases at the national level, and the average down payment was 6% of the purchase price. The median home price for first-time purchasers was \$215,000, about 79% of the median price for all home purchases. Using this information to scale 2020 Michigan data, there would be about 35,500 first-time purchasers, a median home price of \$200,655, and a down payment of about \$12,000.

¹ https://www.michigan.gov/documents/snyder/Senate_Bills_511-512_veto_letter_641856_7.pdf

Because it is likely that participants will save for more than just one year before making a purchase, the annual revenue loss will increase for two or three years as more prospective taxpayers take advantage of the annual exemption. At some point the number of new participants will be balanced by first-time purchasers, and the revenue loss will grow more slowly, primarily due to increases in home prices.

As previously stated, the participation rate and annual savings are the two most critical variables in estimating the fiscal impact, and deviations from the assumed amounts can alter the estimate significantly. An evaluation of tax year 2019 income tax data shows that, for a similar program designed to promote saving for higher education (the Michigan Educational Savings Program), there were roughly 72,700 participants and net income tax revenue was reduced by about \$12.6 million. Given that the MESP is intended as a longer term savings program for higher education expenses, it is reasonable to assume that the revenue loss resulting from a savings program to benefit first-time home buyers would be substantially less.

If the average taxpayer participates for three years before purchasing a home and 20% of each year's first-time homebuyers participate in the program, the revenue loss would stabilize at roughly \$3.0 million on an annual basis. If the exemption reduces the taxpayer's burden such that it creates a larger refund, the revenue impact would fall entirely on the general fund. However, if the taxpayer's liability declines but remains greater than zero, about 23.8% of the revenue loss will be borne by the School Aid Fund, with the remainder coming from the general fund.

ARGUMENTS:

For:

The savings account program proposed in the bills is an ideal vehicle to address the homeownership and down payment challenge in Michigan. The tax benefits—being able to deduct contributions and use qualified withdrawals tax-free—will incentivize individuals to save for down payments, even those who might think of homeownership as an unattainable goal. Survey data from supporters of the bills show that more people would like to buy a home than can afford to do so, and polling indicates that people support the savings account idea, with renters reporting that they would utilize the accounts.

Already, families are able to support education through 529 plans. In a similar way, parents and grandparents would be able to set aside money gradually in a tax-advantaged home buyer savings program to help ease the strain of a single large investment.

For:

The savings account will not only help families save for and invest in homes, but helps the entire state invest in itself. The incentivized accounts will help keep people in Michigan, or even attract people to move here. The state as a whole and individual communities benefit from people who have committed to homeownership in a particular area.

Against:

It may be the case that those most likely to already save for a home—potentially higher income individuals with existing access to bank and savings accounts—will disproportionately utilize the program; low-income individuals may have less opportunity to access the program. In that

sense, the state as a whole—including low-income individuals—will be shouldering the cost of the tax benefit for a few.

Response:

Promoting home ownership is a valuable and achievable state policy goal. Even if there are short-term costs to the tax benefit, the long-term gains—more home owners in Michigan, more stable families, more housing construction—will outweigh those costs.

Additionally, the program is structured so that anyone can access the account: there are no prequalifications or application requirements. In fact, one might expect that middle-income buyers would be most likely to use the savings account program: high-income buyers may simply not need to save at all, and low-income individuals may qualify for other state and federal home ownership assistance programs.

Against:

The state should not rewrite the tax code to incentivize a specific activity that benefits a specific group of individuals. With an overhaul of the state income tax in the early 2010s, Michigan has worked to eliminate specific tax credits and incentives. While saving for a house is no doubt an admirable goal, there are many worthy purposes for saving. What about saving to start a new business? What about saving for medical costs? The state should not be in the business of picking various behaviors that will receive preferential tax treatment.

POSITIONS:

A representative of Michigan Realtors testified in support of the bills. (3-17-21)

The following entities indicated support for the bills:

- Community Economic Development Association of Michigan (3-17-21)
- Lake Trust Credit Union (3-17-21)
- Renovare Development (3-17-21)
- Home Builders Association of Michigan (3-17-21)
- Grand Rapids Chamber (3-17-21)
- Michigan Credit Union League (3-17-21)
- Habitat for Humanity of Michigan (3-17-21)
- Michigan Chamber (3-17-21)
- Michigan Mortgage Lenders Association (3-17-21)
- Detroit Regional Chamber (3-24-21)

A representative of the Department of Treasury testified in opposition to the bills. (3-17-21)

Legislative Analyst: Jenny McInerney
Fiscal Analyst: Jim Stansell

■ This analysis was prepared by nonpartisan House Fiscal Agency staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.