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

BILL ANALYSIS

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

House Bill 4289 (Substitute H-3 as passed by the House)
House Bill 4290 (as passed by the House)
Sponsor: Representative John Damoose (H.B. 4289)
Representative Mari Manoogian (H.B. 4290)
House Committee: Tax Policy
Senate Committee: Finance

Date Completed: 10-27-21

CONTENT

House Bill 4289 (H-3) would enact the "Michigan First-Time Home Buyer Savings Program Act" to do the following:

-- Establish the First-Time Home Buyer Savings Program in the Department of Treasury.
-- Allow an individual, beginning January 1, 2022, to open an account with a financial institution and designate it as a first-time home buyer savings account to be used to pay or reimburse a beneficiary's eligible costs for the purchase of a single-family residence in the State.
-- Specify that contributions to and interest earned on a first-time home buyer savings account, as well as qualified withdrawals made from the account, would be exempt from taxation under the Income Tax Act.
-- Limit the maximum account balance of a first-time home buyer savings account to $50,000, except for accrued earnings.
-- Specify that, subject to certain exceptions, funds withdrawn from an account for any purpose other than the payment of eligible costs would be subject to a penalty equal to 10% of the amount withdrawn.
-- Specify that financial institution would not be responsible or liable for certain duties with respect to a first-time home buyer savings account.
-- Require the Department to prepare forms for account-related items to be filed with an income tax return filed under the Income Tax Act.
-- Allow the State Treasurer to promulgate rules to implement the Program.
-- Allow the Department to prepare and distribute informational materials on the Program to financial institutions and potential home buyers.

House Bill 4290 would amend the Income Tax Act to allow a deduction, per tax year, of up to $5,000 for a single return and $10,000 for a joint return for contributions to a first-time home buyer savings account for up to 20 tax years; and to allow a deduction for qualified withdrawals from an account.

The bills are tie-barred.

House Bill 4289 (H-3)

Definitions

"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. "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.

"First-time home buyer" would mean an individual who is a resident of the State and has not owned or purchased, either individually or jointly, a single-family residence during a period of three years before the date of the purchase of a single-family residence. "Single-family residence" would mean a single-family residence owned and occupied by a qualified beneficiary as his or her principal residence (as that term is defined in the General Property Tax Act). The term would include a manufactured home, trailer, mobile home, condominium, or cooperative.

First-Time Home Buyer Savings Account

The First-Time Home Buyer Savings Program would be established in the Department of Treasury. The purposes, powers, and duties of the Program would be vested in and would have to be exercised by the State Treasurer or his or her designee.

Beginning January 1, 2022, any individual could open an account with a financial institution and designate it, 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 the State. An account holder would have to designate a first-time home buyer as the qualified beneficiary of the account. The account holder could designate himself or herself as the qualified beneficiary and could change the designated qualified beneficiary at any time, but there could not be more than one qualified beneficiary at any one time.

An individual could jointly own a first-time home buyer savings account with another person if the joint account holders filed a joint return under the Income Tax Act. An individual could be the account holder of more than one account. However, an account holder could not have multiple accounts that designated the same qualified beneficiary. An individual could be designated as the qualified beneficiary on more than one first-time home buyer savings account.

Only cash and marketable securities could be contributed to a first-time home buyer savings account. Subject to the limitation on the amount of contributions, people other than the account holder could make contributions to a first-time home buyer savings account.

The account holder would be responsible for the use or application of funds in a first-time home buyer savings account. The account holder could not use funds held in an account to pay expenses of administering the account, although a service fee could be deducted from the account by a financial institution in which the account was held. An account holder could withdraw funds, in whole or in part, from a first-time home buyer savings account and deposit them in a new first-time home buyer savings account held by a different financial institution or the same financial institution. If necessary, an account holder or qualified beneficiary could make a hardship withdrawal from the account due to an immediate and heavy financial need of the account holder or qualified beneficiary. However, the amount withdrawn would have to be limited to the amount necessary to satisfy that need. A hardship withdrawal would not be a qualified withdrawal and would be subject to taxation under the Income Tax Act.

The account balance for a first-time home buyer savings account could not exceed a maximum of $50,000. Accounts could continue to accrue earnings if the total balance had reached the limit and would not be considered to have exceeded the maximum account balance.

Tax Exemption

Contributions to and interest earned on a first-time home buyer savings account, as well as qualified withdrawals made from the account, would be exempt from taxation under Section 30 of the Income Tax Act (the section Senate Bill 146 would amend). "Qualified withdrawal" would mean a withdrawal from an account that is made at least one year after the account was opened and designated as a first-time home buyer savings account and the withdrawal is used to pay the eligible costs of the qualified beneficiary incurred at least one year after the account is designated.

Penalty

If funds were withdrawn from an account for any purpose other than the payment of eligible costs by or on behalf of a qualified beneficiary, there would be a penalty equal to 10% of the amount withdrawn. The penalty would have to be paid to the Department. However, the penalty would not apply if the funds withdrawn satisfied any of the following:

-- Withdrawn by reason of the qualified beneficiary's death or disability.
-- A disbursement of assets of the account under a filing for protection under the United States Bankruptcy Code.
-- Transferred from an account established under the proposed Act into another account established under the Act for the benefit of another qualified beneficiary.
-- Withdrawn by reason of a hardship withdrawal.
-- Withdrawn by reason of qualified beneficiary who was a service member who was transferred or deployed out of the State on active duty under a permanent change of station order and provided proof acceptable to the Department that the qualified beneficiary or his or her spouse was assigned to a duty station outside the State under a permanent change of station order.

"Active duty" would mean active duty pursuant to an executive order of the President of the United States, and act of Congress, or an order of the Governor. "Armed Forces" would mean the term as defined by the Veteran Right to Employment Services Act. "Service member" would mean a member of the Armed Forces, reserve branch of the Armed Forces, or Michigan National Guard.

Document Submission & Department Rules

An account holder would have to submit, with his or her income tax return filed under the Income Tax Act, all of the following to the Department, on forms prescribed by the Department:

-- Account statements that showed the contributions made during the tax year and the taxable interest or earnings on the account in the tax year for which the deduction was claimed.
-- The Form 1099 issued by the financial institution for the account for the tax year for which the deduction is claimed.
-- Upon a withdrawal of funds from a first-time home buyer savings account, a copy of the real estate settlement statement that showed the withdrawal was used for eligible costs.

An account holder would be required to maintain and keep, for a period of at least four years, suitable records and documentation, for each first-time home buyer savings account, including, account statements for all contributions and withdrawals made, a detailed list describing the transactions for the account, and other pertinent records and papers as required by the Department for the administration of the Act.

The Department would have to prescribe the form and manner in which a taxpayer would claim a deduction in accordance with the Act on his or her income tax return. The form would include, at minimum:

-- The account holder's name.
-- The name of the qualified beneficiary.
-- The name of the financial institution and the account number.
-- The beginning and end of the year balance of the account.
-- The amount of the deduction claimed for the tax year.

The State Treasurer could promulgate rules to implement the Program. The rules could not apply to, or impose administrative, reporting, or other obligations or requirements on, financial institutions-related accounts for first-time home buyer savings accounts.

The Department could prepare and distribute informational materials on the First-Time Home Buyer Savings Program to financial institutions and potential home buyers to publicize the availability of the program.

<u>Financial Institutions</u>

A financial institution would not have to do any of the following:

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

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

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

After being furnished proof of the death of the account holder and any other information required by the contract governing the first-time home buyer savings account, a financial institution would have to distribute the principal and accumulated interest or other income in the account in accordance with the terms of the contract.

"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.

House Bill 4290

Under the Income Tax Act, for a person other than a corporation, estate, or trust, "taxable income" means adjusted gross income, as defined in the Internal Revenue Code, subject to various adjustments. For tax years beginning on and after January 1, 2022, the bill would allow a taxpayer to deduct from taxable income all of the following:

-- To the extent not deducted in determining adjusted gross income, contributions made by the taxpayer in the tax year less qualified withdrawals made in the tax year from a first-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.
-- To the extent not deducted in determining adjusted gross income, interest earned in the tax year on the contributions to the taxpayer's first-time home buyer savings account if the contributions were deductible.
-- To the extent included in adjusted gross income, distributions that were qualified withdrawals from a first-time home buyer savings account to the qualified beneficiary of that account.

The calculated amount of contributions less qualified withdrawals could not be less than zero, and the deduction for contributions could not be claimed for more than 20 years.

For tax years that begin on and after January 1, 2022, a taxpayer would have to add to his or her adjusted gross income, to the extent not included in adjusted gross income, the amount of money the taxpayer withdrew in the tax year from the first-time home buyer savings account, not to exceed the total amount deducted in the tax year and all previous tax years, if the withdrawal were not a qualified withdrawal. This provision would not apply to withdrawals that were less than the sum of all contributions made to a first-time home buyer savings account in all previous tax years for which no deduction was claimed, minus any contributions for which no deduction was claimed that were withdrawn in previous tax years.

MCL 206.30 (H.B. 4290) Legislative Analyst: Christian Schmidt

FISCAL IMPACT

The bills would reduce revenue to both the State General Fund and the State School Aid Fund by approximately $1.9 million to $19.8 million per year beginning in fiscal year 2021-22, although the actual amount would depend on actual contributions and participation rates. Approximately 23.8% of any revenue reduction would lower School Aid Fund revenue, with the remaining impact lowering General Fund revenue. The maximum potential revenue loss under the bills is much greater.

The most important variables in estimating the fiscal impact of the bills are the participation rate and the average annual contribution to the accounts. The bills would be more generous than similar proposals introduced or adopted in other states, suggesting that participation could be higher than estimated in other states. However, Michigan already has the fourth-highest homeownership rate in the United States, which could suggest that participation either would be either greater (because homeownership is a higher priority with the population) or lower (because people, comparatively, are purchasing or owning homes at a higher rate already, suggesting that less assistance, like that proposed by the bills, is needed) than in programs in other states. Similarly, Michigan's marginal tax rate is approximately half to two-thirds of the tax rate in other states with similar proposals, meaning that the bills would provide relatively less tax relief than provided by the provisions in other states. The provisions would be on top of any Federal incentives for first-time homebuyers.

Data from the Michigan Association of Realtors indicate that over the 2018-2020 period an average of 114,766 homes were sold each year. National figures indicate that first-time buyers represent 38% of purchasers. If contributions deductible under the bills averaged $5,500, and 8,000 individuals claimed the deduction, the bills would reduce revenue by $1.9 million per year. In 2020, the average sale price totaled approximately $214,000. If 50% of the estimated number of first-time homebuyers saved an average of five years to accumulate enough money in the account to make a 10% down payment on a mortgage for an average-priced home, the bills would reduce revenue by approximately $19.8 million per year by 2026; illustrating the degree to which the fiscal impact of the bills could vary based on participation rates and average contributions.

The bills would result in additional administrative costs to the Department of Treasury. The Department could incur additional administrative expenses from administering the program, processing additional information on income tax returns, and marketing the program. These expenses could be minimal and within current appropriations, though a more accurate estimate is not currently available.

Fiscal Analyst: David Zin

SAS\S2122\s4289sa