

Legislative Analysis



FLOW-THROUGH ENTITY TAX MODIFICATIONS

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

House Bill 5022 (H-2) as reported from committee

Sponsor: Rep. Alabas Farhat

Committee: Tax Policy

Complete to 12-7-24

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

(Enacted as Public Act 216 of 2024)

SUMMARY:

House Bill 5022 would amend the Income Tax Act to change provisions relating to the flow-through entity tax, including the conditions under which penalties and interest are not assessed and the date on which a taxpayer must elect pay the tax.

Electing to pay the flow-through entity tax

Currently, a taxpayer that elects to pay the flow-through entity tax must file their election with the Department of Treasury on or before March 15 of that tax year.

Under the bill, for tax years beginning on or after January 1, 2024, a flow-through entity would be required to file its election with the department before the last day of the ninth month after the end of the tax year.

The bill would also provide that if a person's election to pay the flow-through entity tax is denied by the department, the person could file a written notice with the department within 60 days and be entitled to an informal conference on the question in the same manner as provided in 1941 PA 122.¹

Penalties and interest

Currently, the act requires taxpayers that elect to file under the flow-through entity tax with an expected liability of at least \$800 to file an estimated return and pay the estimated tax in each quarter of the tax year. If the taxpayer's liability for the preceding tax year was less than \$20,000 and the taxpayer made four equal payments equal to the previous year's liability, interest penalties provide under the bill are not assessed.

Under the bill, the following would apply beginning in the 2024 tax year:

- Interest and penalties would not be assessed if the taxpayer submitted four equal payments totaling at least one of the following:
 - 90% of the taxpayer's current year tax liability.
 - 100% of the taxpayer's previous year tax liability.
- Interest and penalties would not be assessed for any quarterly estimated payment due prior to the taxpayer making the election to flow-through entity tax for that tax year, unless the department determines that the deficiency is due to the taxpayer's intentional disregard of the law.

¹ <https://www.legislature.mi.gov/Laws/MCL?objectName=MCL-205-21>

Required disclosures

The act currently requires flow-through entities that do not elect to pay the flow-through entity tax to provide certain listed information to any member the information is required to be provided to by the Internal Revenue Code, including the member's share of the flow-through tax imposed on the taxpayer and paid by the fifteenth day of the third month after the end of the tax year.

The bill would amend this requirement so that, for tax years beginning on or after January 1, 2024, the disclosure must include information about the member's share of the flow-through tax that was paid on or before the date for the filing of the flow-through entities annual return for that tax year, including any extension.

The bill would also newly require that this disclosure be filed in a form and manner prescribed by the Department of Treasury and that it include any other information the department determines to be necessary for the filing of a direct or indirect member's tax return.

Reasonable proof to claim credit

The act currently allows an individual that elects to pay the flow-through tax to claim a credit against their individual or corporate income tax liability for the amount of flow-through tax paid.

The bill would allow the Department of Treasury to require reasonable proof from the taxpayer related to a claimed credit, or any other information required by the department to administer the credit.

MCL 206.254 et seq.

BACKGROUND:

The flow-through entity tax was created, retroactive to the 2021 tax year, by 2021 PA 135. The tax allows flow-through entities (e.g., S corporations or partnerships) to deduct state and local taxes beyond the \$10,000 cap for federal individual income taxes.^{2,3}

According to committee testimony, the bill is intended to address several potential issues that have been found with the current statute during the first years of implementation. Supporters argue that the bill will benefit both tax filers and the Department of Treasury.

FISCAL IMPACT:

House Bill 5022 is not expected to have a significant impact on state revenues or Department of Treasury administrative costs.

POSITIONS:

Representatives of the following entities testified in support of the bill (12-4-24):

- Department of Treasury

² <https://www.michigan.gov/taxes/business-taxes/flowthrough-entity-tax/frequently-asked-questions>

³ <http://legislature.mi.gov/doc.aspx?2021-HB-5376>

- Michigan Association of CPAs

The following entities indicated support for the bill (12-4-24):

- National Federation of Independent Businesses
- Michigan Manufacturers Association

Legislative Analyst: Alex Stegbauer
Fiscal Analyst: Ben Gielczyk

■ 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.