Legislative Analysis

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INCOME TAX RATE REDUCTION

House Bill 4170 as reported from committee
Sponsor: Rep. Kathy Schmaltz
Committee: Finance
Complete to 3-18-25

SUMMARY:

House Bill 4170 would amend the Income Tax Act to reduce the individual income tax rate and make other changes described below.

Individual income tax rate
Currently, the individual income tax rate is 4.25%.

The bill would reduce the rate to 4.05%, effective January 1, 2025.

(Note: The bill would also retroactively codify into statute the temporary tax rate rollback triggered by the provision discussed below.)

Tax rate rollbacks
Currently, the act provides that if the growth in total general fund revenue outpaces inflation in a given fiscal year, the individual income tax rate must be reduced proportionally based on the amount by which revenue growth exceeded inflation.[1]

Previously, this provision was applied to reduce the tax rate to 4.05% for the 2024 tax year.[2] However, the Michigan Court of Appeals ruled that, as the law is written, any rate reduction under the act is temporary and applies only to a single tax year.[3] The Michigan Supreme Court declined to hear an appeal of that decision.

The bill would add language clarifying that, beginning with the 2026 tax year, any rate reduction calculated under the above provision is permanent and becomes the permanent rate for all subsequent tax years, unless another rate reduction is triggered by an increase in general fund revenue.

MCL 206.51

BRIEF DISCUSSION:

Supporters argued that the bill would clarify the legislature's original intent in enacting the rollback provisions and put money back into the pockets of taxpayers and small businesses in doing so. They argued that the best use of that money would be to give taxpayers a break to

[1] https://www.legislature.mi.gov/documents/2015-2016/billanalysis/House/pdf/2015-HLA-4370-3C42FEC9.pdf
[2] https://www.bridgemi.com/michigan-government/michigan-income-tax-cut-not-permanent-court-rules
[3] https://www.michigan.gov/treasury/reference/taxpayer-notices/the-reduction-to-the-income-tax-rate-for-tax-year-2023-was-temporary

deal with the effects of inflation. They also argued that the tax cut would stimulate greater economic activity and could lead to more opportunity for residents and possibly population growth for the state.

Others contended that the same amount of money would have greater impact when aggregated by the state in hundreds of millions of dollars to fund common goods for all residents, such as infrastructure or other projects and programs. They also argued that the benefits of the tax cut would be weighted toward wealthy households, while the average benefit for low- and middle-income residents would be less than the average amount per household cited by the bill's supporters. Finally, they raised concerns that the permanent rollbacks created under the bill would lead to an irreversible march toward income tax elimination, even when the revenue growth triggering a rollback is unrelated to the state's economic health.

Some also raised concerns about the potential impact on the current budget by implementing a tax cut mid-year. Supporters countered that the most recent Consensus Revenue Estimating Conference estimated a surplus for the current fiscal year that would be enough to implement the rate cut this fiscal year without adjusting the current budget.

FISCAL IMPACT:

House Bill 4170 would reduce income tax revenue by approximately $539.3 million in FY 2024-25, which represents three-quarters of the fiscal year due to the rate reduction starting on January 1, 2025; $713.0 million in FY 2025-26; and $727.6 million in FY 2026-27 (based on January 2025 consensus revenue estimating conference (CREC) estimates over the forecast horizon). However, it should be noted that the effective date of the bill's provisions (sometime after the January 1, 2025 start of the rate reduction) would likely result in some portion of the FY 2024-25 rate reduction impact being realized in FY 2025-26 individual income tax refunds. The corresponding revenue reduction in fiscal years beyond FY 2026-27 would be a function of income tax collections. The revenue reduction would only affect general fund collections due to the school aid earmark formula effectively holding the School Aid Fund harmless from any rate reduction.

The bill would also require that any future rate reduction due to the income tax rate reduction trigger provision be permanent and carry forward to future fiscal years. This would reduce revenues by an unknown amount and would depend on future rate reductions. Under current law, an income tax rate reduction under the income tax trigger provision is temporary, lasting only one calendar year.

POSITIONS:

Representatives of the following entities testified in support of the bill (3-11-25):

- National Federation of Independent Businesses
- Morey Fiscal Policy Initiative

The following entities indicated support for the bill (3-11-25):

- Small Business Association of Michigan
- Americans for Prosperity Michigan
- Associated Builders and Contractors of Michigan

- Home Builders Association of Michigan

The following entities indicated opposition to the bill (3-11-25):

- Department of Treasury
- Michigan League for Public Policy
- 482forward
- Student Advocacy Center
- Michigan State Employee Retirees Association
- Up North Advocacy
- Clean Water Action

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■ 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.