



**Senate Fiscal Agency**  
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BILL



ANALYSIS

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Senate Bill 511 (as reported without amendment)  
Senate Bill 512 (Substitute S-1 as reported)  
Sponsor: Senator Peter MacGregor (S.B. 511)  
Senator Ken Horn (S.B. 512)  
Committee: Finance

Date Completed: 11-27-17

### **RATIONALE**

Usually, a house is the most significant purchase a person makes in his or her lifetime. According to Zillow.com, a real estate and rental marketplace website, the median home value in Michigan is \$135,300, and that value is expected to rise 3.8% within the next year. The website also lists the median price of currently listed homes in the State as \$169,900. For a down payment on a home, some recommend that a person make a payment of at least 20% to avoid purchasing private mortgage insurance, which protects a lender from losing money if the purchaser ends up in foreclosure. Regardless of whether a down payment of at least 20% is made, a person often must save a considerable sum of money toward the purchase of a home.

To encourage people to save money to purchase a home in Michigan, some have suggested that the State provide tax incentives through a first-time home buyer savings program. In addition, some believe that such a program would entice educated workers to stay in the State. While Michigan has 15 public four-year universities, as well as a number of community and private colleges, that graduate many students, research suggests that many college-educated people are leaving the State to live and work elsewhere.

### **CONTENT**

**Senate Bill 511 would create the "Michigan First-Time Home Buyer Savings Program Act" to do the following:**

- **Require the Department of Treasury to establish the First-Time Home Buyer Savings Program.**
- **Allow an individual, beginning January 1, 2018, to open an account with a financial institution and designate the account 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 \$100,000, subject to an earnings exception.**
- **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 what a financial institution would not be responsible or liable for, regarding first-time home buyer savings accounts.**
- **Require the Department to prepare forms for certain 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 Michigan First-Time Home Buyer Savings Program to financial institutions and potential home buyers to publicize the availability of the Program.**

**Senate Bill 512 (S-1) 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 allow a deduction for qualified withdrawals from an account.**

The bills are tie-barred.

Under Senate Bill 511, "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). "Single-family residence" would include a manufactured home, trailer, mobile home, condominium, or cooperative.

### **Senate Bill 511**

#### **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 have to be exercised by the State Treasurer or his or her designee.

Beginning January 1, 2018, 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 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 first-time home buyer savings 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 the funds in a new

first-time home buyer savings account held by a different financial institution or the same financial institution.

The account balance for a first-time home buyer savings account could not exceed a maximum of \$100,000. Accounts could continue to accrue earnings if the total balance had reached the limit and could 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 512 would amend).

"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 a withdrawal from an account to pay the eligible costs of the qualified beneficiary incurred after the account is established or a withdrawal made as the result of the death or disability of the qualified beneficiary of an account.

#### 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.

#### 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:

- Detailed information regarding the first-time home buyer savings account, including a list of transactions for the account during the tax year.
- The form 1099 issued by the financial institution for the account.
- Upon withdrawal of funds from a first-time home buyer savings account, a detailed account of the eligible costs toward which the account funds were applied and a statement of the amount of funds remaining in the account, if any.

The Department would have to prepare forms for each of the following to be filed with an income tax return:

- The designation of an account with a financial institution to serve as a first-time home buyer savings account.
- The designation of a qualified beneficiary of a first-time home buyer savings account.
- Detailed information regarding the first-time home buyer savings account, including a list of transactions for the account during the tax year, and identifying any supporting documentation that the account holder was required to maintain, for annual submission to the Department.

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.

## Financial Institutions

A financial institution would not be required 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 would not be otherwise 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.

Upon 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, or similar entity authorized to do business in Michigan.

## **Senate Bill 512 (S-1)**

For tax years beginning after December 31, 2017, 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-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.
- 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.

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.

## **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**

According to Committee testimony, based on a poll of 600 people, the three largest deterrents to first-time homeownership are college debt, making a down payment, and low wages. In addition, 65% of renters polled said they would avail themselves of a savings incentive program. By offering individuals a tax deduction for money set aside to purchase a home, the bills would help mitigate barriers to homeownership and encourage people to save for a home in Michigan.

**Response:** The proposed maximum account balance of \$100,000 is too high, and could be abused by account holders to shelter money from taxes. As stated above, the median home price in the State is estimated to be \$169,900. The maximum account balance should be lowered to approximately 20% of that median price.

### **Supporting Argument**

According to an article from nytimes.com, Midwest states, such as Iowa, Michigan, and Ohio, and some Plains states, such as Nebraska and South Dakota, saw the largest net migration losses in young college-educated people between 2000 and 2015. In contrast, the states that gained college graduates were coastal and southern states, such as California, Maryland, and Texas.

Michigan needs to enact policies that will attract educated talent, or retain graduates of in-State colleges and universities, who are often Michigan natives. According to Committee testimony, other states, such as Colorado, Iowa, Minnesota, Mississippi, Montana, and Virginia, have enacted similar programs. The bills would establish an important tool to encourage people to settle or stay in Michigan, and keep Michigan competitive with other states.

### **Supporting Argument**

Due to the flexible structure of a first-time home buyer savings account, many people could make use of the program. For example, because a savings account could be opened by anyone, the bills would give families or close friends another way to save for a person's future. A parent could open an account for his or her child, just as the parent currently may open a college savings account for the child. Additionally, the bills could encourage a person who was a long-term renter to switch from renting to owning his or her own home. Also, if a person had lost his or her home for some reason, he or she could use the program to save up for another home.

### **Opposing Argument**

By providing an incentive for individuals to save for a home through an income tax deduction, the bills would work in contrast to the policy of limiting the number of exemptions and deductions for taxpayers and not using the tax code to influence taxpayer behavior. The bills also would create some inequity between taxpayers who already own a home or for whom homeownership is not a priority, and could create an administrative burden on the Department of Treasury to operate the program.

### **Opposing Argument**

The bills would reduce tax revenue and, in turn, decrease the money available to pay for State-supported services, such as education.

Legislative Analyst: Drew Krogulecki

## **FISCAL IMPACT**

The bills would reduce revenue to both the State General Fund and the State School Aid Fund by

approximately \$800,000 to \$1.9 million per year, 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 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 might 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 would be either greater (because homeownership is a higher priority with the population) or less (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). 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 less tax relief than other states do.

Data from the Michigan Association of Realtors indicate that 136,177 homes were sold in Michigan in 2016, and 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 2016, the average sale price totaled approximately \$154,000. If 50% 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 \$16.9 million per year; 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.

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.