

Senate Fiscal Agency
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SFA



BILL ANALYSIS

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Senate Bill 1382 (as enrolled)
Sponsor: Senator Bill Bullard, Jr.
Senate Committee: Finance
House Committee: Tax Policy

PUBLIC ACT 400 of 2000

Date Completed: 1-18-01

RATIONALE

Under the Internal Revenue Code, when an individual receives a distribution from an individual retirement account (IRA) or other pension plan, the distribution is added to the individual's income for purposes of calculating Federal adjusted gross income (AGI). If the person directs the distribution to a qualified charity, the taxpayer may deduct the distribution, after calculating AGI, to determine his or her income subject to the Federal income tax. The Michigan Income Tax Act requires a taxpayer to begin the calculation of the State income tax by using his or her Federal AGI. As a result, a taxpayer who transferred a distribution from an IRA to a charity was taxed on the amount of the distribution at the State level, even though he or she had no Federal tax liability on the distribution. It was suggested that the State also allow a taxpayer to deduct distributions to charity that are made from an IRA or other pension plan.

- To a charitable remainder annuity trust or charitable remainder unitrust as defined in Section 664(d) of the IRC. (These trusts are dedicated to certain charitable organizations after a specified period of time, or the death of the individual(s) for whom the trust is formed.)
- To a pooled income fund as defined in Section 642(c)(5) of the IRC (which provides that a pooled income fund is a trust in which each donor can make an irrevocable transfer of property to or for the use of certain charitable organizations).
- For the issuance of a charitable gift annuity as defined in Section 501(m)(5) of the IRC (which describes a charitable gift annuity, in part, as an annuity of which a portion is allowed as a deduction for contributions to certain charitable organizations).

A trust, fund, or annuity described above is a qualified charitable organization only if no person (other than the taxpayer who received the distribution from the retirement or pension plan, the taxpayer's spouse, or a 501(c)(3) organization) holds any interest in the trust, fund, or annuity.

The bill applies to distributions from retirement or pension plans that are qualified pension, trusts, or annuity plans under Section 401(a) of the IRC (which prescribes the requirements for pension plans), including the following:

CONTENT

The bill amended the Income Tax Act to allow a taxpayer to deduct from taxable income, to the extent included in Federal adjusted gross income, certain distributions made from a retirement or pension plan to a charitable organization ("qualified charitable distributions"). The bill applies to tax years beginning after 2000.

The bill defines "qualified charitable distribution" as a distribution of assets to a qualified charitable organization by a taxpayer within 60 days after the date the taxpayer received the assets as a distribution from a retirement or pension plan. A distribution is to a qualified charitable organization if it is made under any of the following circumstances:

- To a 501(c)(3) organization, other than an organization that is controlled by a political party, an elected official, or a candidate for an elective office. (Section 501(c)(3) of the Internal Revenue Code (IRC) exempts from taxation certain charitable organizations.)

- Plans for self-employed persons (Keogh or HR 10 plans).
- Individual retirement accounts if distributions are not made until the participant has reached age 59½ years, except in the case of death, disability, or other distributions described in the IRC.
- Employee annuities or tax-sheltered annuities purchased by public school systems, or by organizations exempt from taxation under Section 501(c)(3) of the IRC.
- Distributions from a 401(k) plan attributable to employee contributions mandated by the plan or attributable to employer contributions.

deduct such distributions, to the extent they are included in AGI, the bill makes the State tax treatment of charitable gifts more equitable.

Legislative Analyst: G. Towne

FISCAL IMPACT

The bill will reduce income tax revenue an estimated \$0.7 million in FY 2000-01 and \$1.3 million in FY 2001-02. The loss in revenue primarily will affect General Fund/General Purpose revenue.

Fiscal Analyst: J. Wortley

The amount a taxpayer may deduct under the bill is equal to the amount deductible by the taxpayer under Section 170(c) of the IRC with respect to the qualified charitable distribution in the tax year in which the taxpayer makes the distribution to the qualified charitable organization, reduced by deductions the taxpayer claimed for retirement or pension benefits (except Social Security benefits), and by two times the total amount of credits claimed for contributions to community foundations, food banks, and other specified charitable entities. (Section 170(c) defines "charitable contribution" as a contribution or gift to various specified entities, including the United States, state and local governments, and charitable organizations.)

MCL 206.30

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

Because of the interaction between the Income Tax Act and the IRC, people who directed distributions from an IRA or other pension plan to a qualified charity were not taxed on the distribution for Federal tax purposes, but were subject to the State income tax on those amounts. For instance, if a taxpayer receives a \$2,000 distribution from an IRA, the \$2,000 must be added to the taxpayer's income to determine his or her Federal AGI. If the \$2,000 is given to a qualified charity, the taxpayer can deduct that amount from AGI when calculating his or her taxable income, meaning that the taxpayer has suffered no tax penalty for transferring the amount from the IRA to the charity. For State income tax purposes, however, since calculation of State income tax liability begins with AGI, the \$2,000 was still included, meaning that the taxpayer was taxed on the charitable gift. This created a disincentive for Michigan taxpayers to use IRA or other distributions for charitable purposes. By allowing a taxpayer to

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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.