



**House
Legislative
Analysis
Section**

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**WITHHOLDING INCOME TAX FROM
UI BENEFITS**

**House Bill 5865 (Substitute H-1)
First Analysis (5-15-96)**

**Sponsor: Rep. Edward LaForge
Committee: Human Resources and Labor**

THE APPARENT PROBLEM:

On December 8, 1994, the president of the United States signed into law Public Law 103-465, the so-called "GATT" (General Agreement on Tariffs and Trade) agreement. Under the act, states are required to deduct and withhold federal income tax from unemployment compensation if the person receiving unemployment benefits so elects; states also may withhold state and local income taxes if the individual also so elects. If a state has not enacted legislation conforming to these federal provisions by January 1, 1997, employers in that state would not be able to claim a 5.4 percent credit on their federal taxes. Legislation has been introduced that would mirror the federal legislation in state law.

THE CONTENT OF THE BILL:

The bill would amend the Michigan Employment Security Act by adding a new section that would bring the state into conformity with certain federal requirements. More specifically, the bill would require that beginning January 1, 1997, when people filed new claims for unemployment benefits they would be advised that (a) unemployment benefits are subject to federal and state income tax, (b) some taxpayers are required to make estimated tax payments, (c) the individual may choose to have both federal and state income tax deducted and withheld from his or her unemployment compensation payments, and (d) previously elected withholding status could be changed only once each benefit year. If someone elected to have income tax withheld from unemployment compensation payments, they would have to have both federal and state income tax withheld; people would not be allowed to have only federal or only state income tax withheld.

If someone elected to have money deducted and withheld from his or her unemployment compensation payments, the Michigan Employment Security Commission (MESC) would withhold taxes in the same way as employers are required to do under the Internal Revenue Code. The MESC would be required to

follow all procedures pertaining to the deducting and withholding of income tax specified by the federal Department of Labor, the Internal Revenue Service, and the Michigan Department of Treasury.

Amounts could be deducted and withheld under the bill's provisions only after the claimant's weekly benefit rate had been reduced by the act's pension reduction and earnings offset requirements and adjusted by amounts withheld to satisfy certain legal obligations (restitution, fraud penalties, child support obligations, and necessities). Amounts deducted and withheld from unemployment benefits would remain in the Unemployment Insurance Trust Fund until transferred, as a payment of income tax, to the federal Internal Revenue Service or the state Department of Treasury.

MCL 421.27b

FISCAL IMPLICATIONS:

Fiscal information is not available. (5-14-96)

ARGUMENTS:

For:

Many people who apply for unemployment insurance are not aware that unemployment benefits are treated as income for purposes of federal and state income taxes. As a result, if they don't make provisions to withhold or save part of their benefits, they may be in for an unpleasant shock when their income tax bills fall due. Federal law further requires that states enact legislation notifying unemployment insurance claimants of the option of having federal income taxes withheld from their unemployment benefits. If a state fails to enact such legislation by January 1, 1997, employers would lose a 5.4 percent federal tax credit that they currently can claim and that reduces their taxes from 6.2 percent to 0.8 percent. The bill would implement the necessary legislation, thereby helping both employers and people on unemployment.

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POSITIONS:

The Michigan Employment Security Commission supports the bill. (5-14-96)

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.