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STATE EARNED INCOME CREDIT

House Bill 4189 (Substitute H-1) First Analysis (2-27-97)

Sponsor: Rep. John Freeman
Committee: Tax Policy

THE APPARENT PROBLEM:

The federal earned income tax credit provides low and moderate income working people with a credit that reduces the tax they owe and that can provide a refund even when those filing do not owe any tax. (In a sense, it can be a form of negative income tax.) The credit is available, generally speaking, to a person with taxable and nontaxable earned income of less than \$25,078 (if he or she has at least one qualifying child) or \$28,078 (with more than one child). It is also available to a taxpayer without a qualifying child with income of less than \$9,500. There is a table in the federal tax instruction booklet that indicates the size of the credit based on income. For example, a taxpayer with income of \$15,000, with two children, would be entitled to a credit of \$2,847. (The maximum credit for a taxpayer with one child is \$2,152 and for a taxpayer with more than one child, \$3,556. The maximum for a person without children is \$323.) The credit was created in 1975 and was expanded in 1986, 1990, and 1993. It is described as a means of encouraging lower income persons to work and supplementing low wages. According to testimony before the House Tax Policy Committee, seven states have their own earned income tax credits, which are set at a level equal to a percentage of the federal credit. Legislation has been introduced that would create a state earned income tax credit in Michigan.

THE CONTENT OF THE BILL:

The bill would amend the Income Tax Act to allow a taxpayer, beginning with the 1997 tax year, to claim a refundable credit equal to 10 percent of the Earned Income Tax Credit the taxpayer is allowed to claim for federal tax purposes.

MCL 206.266

FISCAL IMPLICATIONS:

The House Fiscal Agency has estimated the cost of the bill at \$76 million annually. (2-26-97)

ARGUMENTS:

For:

Supporters of this new credit say that it would provide: additional income to families as income from work increases and welfare benefits decline; a wage supplement for people in low-wage jobs; a reduction in poverty among children, since most poor children live in families with one or both parents working; and significant income tax relief for the working poor. The credit provides an incentive to work and is pro-family.

Against:

Some people believe there is a better way to provide tax relief to low-income people. For example, raising the poverty threshold (the income level at which taxes must be paid) would be a more reasonable and straightforward approach. Some people believe that any state EIC should only be available to taxpayers with children.

Against:

A great many tax reduction proposals are afloat. It would make sense to look at them comprehensively rather than piecemeal. It would also make sense to coordinate the review of tax reduction proposals with budget deliberations, so that the full impact of revenue reductions could be understood, including the impact on school funding.

Response:

Supporters of this and other related proposals say that the tax cuts can be paid for out of anticipated revenue growth for the 1998 fiscal year. Further, they say that there have been numerous tax cuts in recent years, many of which have not benefitted the people targeted by the tax cut provided by this bill, low-income working families.

POSITIONS:

Among those who indicated support for the bill before the House Taxation Committee were the Michigan Catholic Conference, the Michigan Family Forum, the Michigan League for Human Services, the Michigan 4C

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Association, and the Michigan Association for the Education of Young Children. (2-26-97)

■ 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.

A representative of the Department of Treasury testified that the administration opposes bills proposing tax reductions until the 1998 fiscal year budget is completed. (2-26-97)

The Michigan Education Association indicated opposition to the bill. (2-26-97)

Analyst: C. Couch
