Legislative Analysis

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EARNED INCOME TAX CREDIT

Senate Bill 453 (Substitute S-5)
Sponsor: Sen. Nancy Cassis
House Committee: Referred Directly to the House Floor
Senate Committee: Finance (Discharged)

Complete to 9-1-06

A SUMMARY OF SENATE BILL 453 AS PASSED BY THE SENATE 8-30-06

The bill would amend the Income Tax Act (MCL 206.272) to allow taxpayers, for tax years beginning after December 31, 2007, to claim a refundable credit against the state income tax equal to a portion of the amount of their federal Earned Income Tax Credit for the same tax year, as follows:

- The credit would be 10 percent of the EITC for the 2008 tax year.
- The credit would be 20 percent of the EITC for the 2009 tax year and beyond.

The bill is tie-barred to Senate Bill 1364 and House Bill 6213, bills which address minimum wage and overtime issues.

FISCAL IMPACT:

The bill can be expected to reduce income tax revenue by an estimated $136.0 million in FY 2008-09 and $300.0 million in FY2009-10. To the extent that the EITC reduces gross income tax collections, it is possible that there could be some small impact on the School Aid Fund. However, the vast majority of the impact would be to reduce GF/GP revenue.

In the 2004 tax year, 662,912 Michigan federal tax returns claimed $1,169,292 in credits.

BACKGROUND INFORMATION:

Established in 1975, the federal Earned Income Tax Credit provides a refundable credit to low-income individuals and families to offset the burden of Social Security taxes, provide an incentive to make the transition from welfare to work, and to supplement earnings. The credit is equal to a percentage of the taxpayer's earned income based on the number of children in the household, up to a certain amount annually adjusted for inflation, as shown in the table below. The maximum credit for the 2006 tax year will be $412 with no qualifying children, $2,747 with one qualifying child, and $4,536 with two or more qualifying children. Generally speaking, to be eligible for the credit, a taxpayer must have earned income (wages, salaries, tips, etc) within specified limits, and have investment income of less than $2,800. If the taxpayer does not have any qualifying children, the taxpayer must be between 25 and 65 years of age. Under federal law, a "qualifying child" is a taxpayer's son, daughter, stepchild, eligible foster child, brother, sister, half or step sibling, or any descendent of them (i.e. grandchild or niece or nephew) who is less than 19 years of age, less than 24 years of age if a student, or of any age if totally and permanently disabled.

The bill applies to tax years beginning in 2008 and, accordingly, the income and credit limits will be higher than the limits for 2006 when adjusted for inflation.

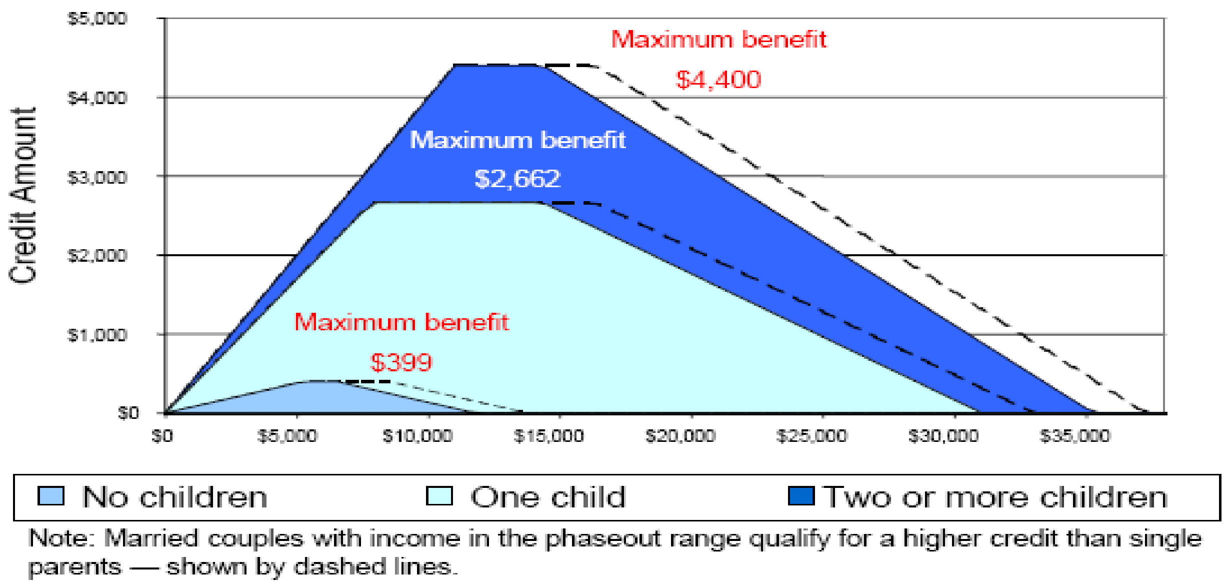
Table 1

				Phase-out Range	
Tax Year	**Credit Percentage**	**Maximum Credit**	**Phase-out rate**	**Single/Head of Household**	**Married filing jointly**
2+ Qualifying Children					
2005	40% of first 11,000	$4,400	21.06%	$14,370 to $35,263	$16,370 to $37,263
2006	40% of first 11,340	$4,536	21.06%	$14,810 to $36,348	$16,810 to $38,348
1 Qualifying Child					
2005	34% of first 7,830	$2,662	15.98%	$14,370 to $31,030	$16,370 to $33,030
2006	34% of first 8,080	$2,747	15.98%	$14,810 to $32,001	$16,810 to $34,001
No Qualifying Children					
2005	7.65% of first $5,200	$399	7.65%	$6,530 to $11,750	$8,530 to $13,750
2006	7.65% of first $5,370	$412	7.65%	$6,740 to $12,120	$8,740 to $14,080

Source: Ami Nagle and Nicholas Johnson, "A Hand Up: How State Earned Income Tax Credits Help Working Families Escape Poverty in 2006." Center on Budget and Policy Priorities. March 2006. The information concerning credit and income limits was modified based data from the IRS Revenue Procedure 2005-70 November 21, 2005).

The chart below shows the amount of the credit based on income levels.

Chart 1



Source: Ami Nagle and Nicholas Johnson, "A Hand Up: How State Earned Income Tax Credits Help Working Families Escape Poverty in 2006." Center on Budget and Policy Priorities. March 2006.

According to a recent report of the Center on Budget and Policy Priorities, 19 other states have an EITC that piggybacks on the federal credit, shown in the table below.

State	**Percentage of Federal Credit**
Colorado	10%
Delaware	20% (in 2006)
District of Columbia	35%
Indiana	6%
Illinois	5%
Iowa	6.50%
Kansas	15%
Maine	4.92%
Maryland	20%
Massachusetts	15%
Minnesota	Average 33%
New Jersey	20%
New York	30%
Oklahoma	5%
Oregon	5% (6% in 2008)
Rhode Island	25%
Vermont	32%
Virginia	20% (in 2006)
Wisconsin	4% (1 Child), 14% (2 Children), 43% (3 Children)

Source: Ami Nagle and Nicholas Johnson, "A Hand Up: How State Earned Income Tax Credits Help Working Families Escape Poverty in 2006." Center on Budget and Policy Priorities. March 2006.

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