
Michigan League for Human Services



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Rewarding Work and Helping Families: Why a State Earned Income Credit Makes Sense for Michigan

Seventeen states and the District of Columbia have established an Earned Income Tax Credit (EITC) to reward the work of low and middle-income families. This analysis outlines the advantages of enacting a Michigan earned income tax credit. It draws on three principles: the need for tax relief for Michigan's working families, the effectiveness of the federal EITC, and the feasibility of a refundable Michigan EITC.

— The Need for Relief for Michigan's Working Families —

Over the last three decades, several factors have increased living expenses, eroded earning power, and decreased job security for many of Michigan's families. As a result, Michigan surpassed all other states from the late 1970s to the mid-1990s in the growth of the number of low-income working families, and currently 13.4 percent of all children in Michigan live in poverty. Decreased job security has also meant that many families not officially considered poor are continually at risk of falling below the poverty threshold, while many others who remain above the threshold are unable to achieve economic self-sufficiency and rely on various forms of government aid.

Factors contributing to hardships for Michigan working families include:

- Changes in Michigan's economy over the last two decades have contributed to the growth in part-time, temporary, and low-wage jobs, replacing many of the well-paying and secure manufacturing jobs that were traditionally a cornerstone of the state economy. As a result, a large number of parents work for low hourly wages or work only part time, and are thus unable to lift their families out of poverty.
- Federal and state welfare legislation, combined with a high demand for entry-level workers, has

resulted in an unprecedented number of welfare recipients moving from public assistance to the work force. In many ways this can be seen as a positive trend. However, the path from welfare to work often leads to dead-end or unstable employment in the low-wage labor market. This is particularly a problem in areas with high unemployment, and also for former recipients who do not have access to skill-building opportunities or who lack transportation to better paying jobs.

- Wages erode each year that the minimum wage is not adjusted for inflation. The inflation-adjusted value of the current minimum wage (\$5.15) is 28 percent lower today than it was in 1979 and 32 percent less than what it was in 1968, and is equal to approximately \$4.56 in 2000 dollars. Moreover, a full-time minimum wage salary (\$10,712) falls far short of the federal poverty threshold for a single parent with two children (\$15,219) or a two-parent family with two children (\$19,157). The maximum federal EITC benefit does not fully offset the inadequacy of the minimum wage, and Michigan's tax on a family of three with minimum-wage earnings is the seventh highest in the nation.

- Federal payroll taxes constitute a larger percentage of a low-income worker's paycheck than that of a middle- or upper-income worker, generally averaging about seven percent of gross pay.
- Work supports such as the federal EITC, child care subsidies, public health insurance and food assistance tend to drop off sharply as family income rises. The loss of benefits becomes especially acute as families reach the poverty threshold.

Michigan's tax policies do little to address the economic challenges facing working families, and in some cases directly contribute to those challenges:

- Although the federal government removed families with incomes below the poverty level from federal income taxation more than a decade ago, Michigan continues to levy income taxes on families well below the poverty level. As a result, in tax year 2002 Michigan's income tax threshold (the point at which a family starts paying state income tax) for a family of four was the 7th lowest in the country, at \$13,200, while the estimated

poverty threshold for that year was \$18,394.¹ This is despite a recent increase in the state's personal exemption.

- Michigan's flat-rate income tax places a disproportionately heavy tax burden on poor working families in the state.
- The increased sales tax resulting from passage of Proposal A in 1994 has particularly hit low-income families, as many non-food necessities have low price-elasticity and must be purchased regardless of their expense.
- While Michigan does offer several tax credits to working poor families, they do not necessarily benefit all low-income households. For example, the Home Heating Credit—through which Michigan distributes federal Low Income Home Energy Assistance Program (LIHEAP) benefits—is only available to households with income under 110 percent of the federal poverty level. Likewise, the tax cut enacted in 1999 reduced the tax burden by a paltry \$25 per year for a family of four earning \$20,000, compared to eight times that amount for a family earning \$100,000.

— The Federal Earned Income Tax Credit —

In any discussion of the implementation of a state EITC, it is worthwhile to examine the federal EITC and its effectiveness in helping working families.

History

In 1975, the federal Earned Income Tax Credit was created by Congress with strong bipartisan support, to help offset the Social Security payroll tax and to make work more attractive than welfare. It has since been expanded three times. In the 1986 Tax Reform Act, its phase-in and phase-out ranges were increased, and a larger credit was provided for families with two or more children. In 1991, the EITC was no longer counted in determining eligibility for most means-tested programs, and was extended to taxpayers with children who did not live with them for the entire year (but at least six months), regardless of who provided child support. In 1994 a small credit was made available to low-income families without children.

Structure

The current federal tax credit has three ranges: 1) the phase-in range where EITC benefits increase with earnings; 2) the flat range where the maximum EITC amount remains constant; and 3) the phase-out range where the maximum EITC benefit is reduced as earnings increase. For example, for tax year 2004, a single working parent with one child received a tax credit of approximately 34 percent for every dollar earned up to \$8,000. The same working parent received the maximum credit of \$2,604 if his or her earnings range from \$8,000 to \$14,000. The benefit phase-out range began for the single parent with one child at \$14,000 in earnings, with the benefit percentage being reduced until it was totally exhausted at an income of \$30,000.

Beginning in tax year 2002, the federal EITC benefit scale was modified to distinguish between married and single filers. This is to partially alleviate

¹ The poverty threshold figure is a Family Independence Agency Policy Analysis and Program Evaluation projection (January 16, 2003).

an unintended “marriage penalty” that occurs for some couples, due to the fact that married couples must file a joint return to claim the EITC and the benefit amount is determined by the combined income of both spouses. As a result, there are presently six categories of EITC filers, each with a separate tax credit rate.²

How Refunds Are Spent

Taxpayers who receive the earned income credit have the option of either having it appear as a credit on their paychecks during the year or receiving it as a lump sum after filing their tax forms for that year. Despite the fact that receiving the credit during the year would make the amount of their paychecks higher, most workers opt for the lump sum. This may be due in part to a lack of outreach by the federal government and employers

The IRS has estimated that about half of the federal EITC dollars go to working families with incomes below the official poverty line for a family of four.

to inform workers of all options available, or may reflect a desire among tax filers to receive the credit as a lump sum and apply it toward a major purchase such as an appliance or car repair. Additionally, it is possible that some for-profit tax assistance providers discourage individuals from having the refund appear on their paychecks throughout the year, as it results in a smaller lump-sum payment and hence a lower fee received by the tax company.³

A study by the Center for Policy Research at Syracuse University found that almost half of recipients of the EITC had plans to use all or part of their

Fig. 1

U.S. Treasury Projections of Federal EITC Costs	
Fiscal Year	Cost (millions)
2002	\$32,280
2003	\$35,540
2004	\$36,470
2005	\$37,370
2006	\$38,860
2007	\$40,060
2008	\$41,170

Source: Budget of the United States Government, FY 2004: Analytical Perspectives, Table 6-1.

refund for “making ends meet” (such as paying for utilities or rent, or to a lesser degree, food or clothing), while slightly more than half planned to use all or part of their refund for a “social mobility” use (such as purchasing a car, moving to a safer neighborhood, or paying for tuition). As expected, the lowest income households in the phase-in range had higher immediate needs than did those in the phase-out range, while expenditures for tuitions increased slightly as income rose. Moving, transportation and

savings all peaked in the plateau range and declined slightly in the phase-out range. Almost one-half of all the filers in the study stated that they would save some or all of their EITC check.

Benefits to Michigan

The federal earned income credit has benefited Michigan’s low-income families because it encourages work and is an effective anti-poverty tool. The IRS has estimated that about half of the federal EITC dollars go to working families with incomes below the official poverty line for a family of four. Because it boosts the incomes of working, low-income families without creating additional bureaucratic red tape, it provides highly targeted tax relief at lower administrative cost than other methods for reducing taxes for specific populations (such as the personal exemption or standard deduction). Additionally, the federal credit has provided a boost to Michigan’s economy by bringing federal dollars into local areas where they will be spent. Federal dollars are generally thought to turn around several times in a local economy, and such an influx of those dollars once a year into local areas has given a boost to many small local businesses.

² The categories are: workers not raising a child (not married), workers not raising a child (married), workers raising one child (not married), workers raising one child (married), workers raising two or more children (not married), workers raising two or more children (married).

³ A significant number of low-income filers receive assistance with completing their tax forms from for-profit or non-profit tax assistance services. While the non-profit assistance providers are usually community-based and perform the service for free, the for-profit tax assistance outfits (which may be national chains such as H & R Block, or local small businesses) charge a fee, and often charge extra for a “rapid refund loan” that allows the filer to receive the refund considerably sooner than if the filer waits for a check from the IRS.

— A State Earned Income Credit for Michigan —

While the federal earned income credit has been very beneficial in helping low-income families, many families continue to struggle. One way to effectively augment the success of the federal credit would be to implement a statewide earned income credit, as a growing number of other states are doing. Supplementing wages through a Michigan credit would help to relieve some of the financial pressures on low-income families, by rewarding work and encouraging employment. It may also help to further stimulate local economies.

What a Michigan Earned Income Tax Credit Might Look Like

Michigan, in implementing an earned income credit, would need to address several design issues. These include eligibility, the level of tax relief desired, whether the credit would be refundable or non-refundable, and whether to base the state credit on the federal

EITC (and if so, what the relationship between the two credits would be).

Currently, seventeen states and the District of Columbia now offer state EITC's, twelve of which are refundable. (A refundable tax credit is one in which a family receives the full amount of the credit that exceeds the family's income tax liability.) Two local governments, Montgomery County, Maryland, and Denver, Colorado, offer local EITC's as well.

States with EITC's generally base their eligibility criteria on that of the federal credit; in other words, all families who qualify for the federal credit will qualify for the state credit. Additionally, all state EITC's are currently calculated as a percentage of the federal credit, which makes them efficient to administer. Figure 2 shows the state EITC's currently in place and at what percentage of the federal credit they are calculated.

Fig. 2

State Earned Income Tax Credits Based on the Federal EITC		
State	When Enacted	Percent of Federal Credit
Refundable credits:		
Colorado*	1999	10%
District of Columbia	2000	35%
Illinois	2000 (became refundable in 2003)	5%
Indiana	1999 (based on federal EITC as of 2003)	6%
Kansas	1998	15%
Maryland	1987 (became refundable in 1998)	50% non-refundable, 20% refundable**
Massachusetts	1997	15%
Minnesota	1991	Varies with earnings; average 33%
New Jersey	2000	20% if income below \$20,000
New York	1994	30%
Oklahoma	2002	5%
Vermont	1988	32%
Wisconsin	1989	4% one child, 14% two children, 43% three or more children
Non-refundable credits:		
Iowa		6.5%
Maine	2000	4.92%***
Oregon	1997	5%
Rhode Island	1986	25% (5% refundable)
Virginia	2004	20%

*Based on surplus revenue; suspended since 2002 and will likely be suspended for Tax Year 2005. **Taxpayers may claim either the refundable or non-refundable credit, but not both. ***Maine's EITC will return to 5% in 2006.

Source: State EITC Online Resource Center; Center on Budget and Policy Priorities

In pegging its state earned income credit to the federal credit, Michigan would have a wide range of options regarding the percentage. Factors determining the size of the credit include how much the state is willing to spend on the credit and how much tax relief it wants to target toward low-

income workers. Figure 3 identifies the potential State EITC benefit that would be available to families at various income levels, depending upon whether the credit is based on 25, 10 or 5 percent of the federal credit:⁴

Fig. 3

State EITC Benefits for Tax Year 2004 at Various Income Levels				
State EITC Benefits for Workers Raising One Child				
Total Family Wages	Federal EITC	State EITC at Percent of the Federal Credit		
		25%	10%	5%
• \$5.15/hour (\$10,712/year) [minimum wage]	\$2,604	\$651	\$260	\$130
• \$6.26/ hour (\$13,020/ year) [poverty threshold for singleparent with one child]	\$2,604	\$651	\$260	\$130
• \$7.31/ hour (\$15,205/ year) [poverty threshold for married couple with one child]	\$2,532	\$633	\$253	\$127
• \$10/ hour (\$20,800/ year) [single parent]	\$1,494	\$374	\$149	\$75
• \$10/ hour (\$20,800/ year) [married couple]	\$1,654	\$414	\$165	\$83
• \$12/ hour (\$24,960/ year) [single parent]	\$855	\$214	\$86	\$43
• \$12/ hour (\$24,960/ year) [married couple]	\$1,014	\$254	\$101	\$51
State EITC Benefits for Workers Raising Two or More Children				
Total Family Wages	Federal EITC	State EITC at Percent of the Federal Credit		
		25%	10%	5%
• \$5.15/ hour (\$10,712/year) [minimum wage]	\$4,300	\$1,075	\$430	\$215
• \$7.32/ hour (\$14,494/ year) [poverty threshold for single parent with two children]	\$3,999	\$1,000	\$400	\$200
• \$9.21/ hour (\$18,244/ year) [poverty threshold for married couple with two children]	\$3,367	\$842	\$337	\$168
• \$10/ hour (\$20,800/ year) [single parent]	\$2,840	\$710	\$284	\$142
• \$10/ hour (\$20,800/ year) [married couple]	\$3,051	\$763	\$305	\$153
• \$12/ hour (\$24,960/ year) [single parent]	\$1,998	\$500	\$200	\$100
• \$12/ hour (\$24,960/ year) [married couple]	\$2,209	\$552	\$221	\$110

Source: Michigan League for Human Services.

⁴All calculations are based on 40 hours/52 weeks per year. Poverty thresholds are U.S. Census figures last revised on February 26, 2003.

Cost and Efficiency of a Michigan EITC

The EITC is a tax policy that “makes work pay” and could easily be incorporated into Michigan’s tax code. Because a refundable Michigan EITC would be pegged to the federal EITC, it would be efficiently targeted, would not require a new administrative bureaucracy, and could be easily administered through the current tax system.

Figure 4 shows the estimated cost for a state earned income tax credit in Michigan. It is based on published Internal Revenue Service data on the amount of federal EITC claims filed by residents of Michigan.

Fig. 4

How Much Would a Refundable Michigan EITC Cost? (dollars in millions)							
Federal EITC Claims in Michigan Tax Year 2000		Percent of Total U.S. Claims		Estimated Cost of Federal EITC in FY 2004 (Michigan)			
\$880		2.77%		\$1,011			
Estimated Cost of Michigan EITC, FY 2004*							
Set at 5% of federal credit	Set at 10% of federal credit	Set at 15% of federal credit	Set at 20% of federal credit	Set at 25% of federal credit	Set at 30% of federal credit	Set at 35% of federal credit	Set at 40% of federal credit
\$45	\$91	\$136	\$182	\$227	\$273	\$318	\$364

*Estimates of state EITCs assume participation rate equal to 90 percent of federal participation.

Sources: *Internal Revenue Service; Budget of the United State Government - FY 2004, Analytical Perspectives, pg. 105; Center on Budget and Policy Priorities.*

Prepared by Michigan League for Human Services

Benefits to Local Areas of a State EITC

Available data show that the benefits of enacting a Michigan EITC would be spread throughout the state, and that each county would reap financial rewards in the form of state dollars being returned to local economies. Kent County, for example, would see an influx of more than \$5.6 million in state dollars with a Michigan EITC based on 10 percent of the federal credit, and an influx of more than \$14 million if it is based on 25 percent of the federal credit. Because EITC claimants often spend their refund on such things as appliances, home improvement, clothing, or automobiles and repairs, a state EITC could function as an economic development tool for strengthening local businesses.

Figure 5 shows, county by county, how many residents would benefit from a Michigan EITC and

how much money would be added to local economies.

Bipartisan Support for a Michigan EITC

The federal and state EITC’s that exist today do so because of bipartisan support. The earned income tax credit helps low-income families through supporting and encouraging work. It is seen as an anti-poverty tool, as a way to ensure that workers are not raising their children in poverty, and as an important building block for welfare reform that places a primary emphasis on work over welfare. As such, it has appealed to legislators with a wide range of viewpoints on poverty and public assistance. In Michigan, both Republicans and Democrats have sponsored proposals for a state EITC.

Local Impact of a State Earned Income Credit in Michigan

County	Eligible Households <i>(based on receipt of Federal EITC in Tax Year 2002)</i>		If based on 25% of Federal EITC...		If based on 10% of Federal EITC...	
	Number	Percent of total returns	Average benefit per household	Total added to county economy	Average benefit per household	Total added to county economy
Michigan	601,575	14%	\$425.91	\$256,217,186	\$170.36	\$102,486,874
Alcona	760	16%	\$403.59	\$306,728	\$161.44	\$122,691
Alger	554	13%	386.74	214,254	154.70	85,702
Allegan	5,365	13%	406.99	2,183,512	162.80	873,405
Alpena	2,225	16%	391.55	871,193	156.62	348,477
Antrim	1,542	15%	424.50	654,585	169.80	261,834
Arenac	1,249	19%	404.59	505,337	161.84	202,135
Baraga	580	18%	398.10	230,898	159.24	92,359
Barry	2,459	11%	399.84	983,197	159.93	393,279
Bay	7,029	14%	406.47	2,857,070	162.59	1,142,828
Benzie	1,051	14%	397.28	417,545	158.91	167,018
Berrien	13,178	17%	442.22	5,827,628	176.89	2,331,051
Branch	3,047	16%	403.14	1,228,361	161.26	491,344
Calhoun	10,143	16%	426.07	4,321,618	170.43	1,728,647
Cass	3,131	17%	415.38	1,300,548	166.15	520,219
Charlevoix	1,800	14%	413.34	744,011	165.34	297,605
Cheboygan	2,099	17%	416.21	873,635	166.49	349,454
Chippewa	2,577	17%	408.12	1,051,732	163.25	420,693
Clare	2,765	20%	416.91	1,152,757	166.76	461,103
Clinton	2,101	9%	394.54	828,929	157.82	331,572
Crawford	1,005	19%	428.87	431,017	171.55	172,407
Delta	2,605	15%	391.27	1,019,249	156.51	407,700
Dickinson	1,711	13%	397.22	679,641	158.89	271,856
Eaton	5,448	10%	399.14	2,174,516	159.66	869,806
Emmet	1,927	12%	396.39	763,839	158.56	305,536
Genesee	34,476	17%	445.63	15,363,596	178.25	6,145,438
Gladwin	1,904	17%	416.29	792,620	166.52	317,048
Gogebic	1,096	16%	383.52	420,337	153.41	168,135
Grand Traverse	5,110	11%	384.64	1,965,533	153.86	786,213
Gratiot	2,906	16%	422.97	1,229,154	169.19	491,662
Hillsdale	3,079	16%	403.95	1,243,765	161.58	497,506
Houghton	2,106	14%	377.83	795,702	151.13	318,281
Huron	2,290	14%	395.83	906,456	158.33	362,582
Ingham	17,091	13%	409.84	7,004,534	163.94	2,801,814
Ionia	3,463	13%	398.63	1,380,448	159.45	552,179
Iosco	2,093	17%	406.71	851,250	162.69	340,500
Iron	894	16%	361.16	322,877	144.46	129,151
Isabella	3,045	13%	392.55	1,195,323	157.02	478,129
Jackson	9,980	14%	419.31	4,184,719	167.72	1,673,888
Kalamazoo	11,420	12%	392.45	4,481,730	156.98	1,792,692
Kalkaska	1,160	19%	435.88	505,616	174.35	202,246

Source: Calculations by Michigan League for Human Services based on Brookings Institution analysis of Internal Revenue Service data.

Local Impact of a State Earned Income Credit in Michigan (Cont'd.)

County	Eligible Households <i>(based on receipt of Federal EITC in Tax Year 2002)</i>		If based on 25% of Federal EITC...		If based on 10% of Federal EITC...	
	Number	Percent of total returns	Average benefit per household	Total added to county economy	Average benefit per household	Total added to county economy
Kent	33,704	13%	\$419.50	\$14,138,934	\$167.80	\$5,655,573
Keweenaw	134	15%	325.18	43,575	130.07	17,430
Lake	951	22%	417.44	396,982	166.97	158,793
Lapeer	4,013	11%	404.13	1,621,794	161.65	648,717
Leelanau	777	10%	383.82	298,228	153.53	119,291
Lenawee	5,413	12%	404.71	2,190,708	161.88	876,283
Livingston	3,830	6%	358.50	1,373,058	143.40	549,223
Luce	451	17%	414.65	187,009	165.86	74,804
Mackinac	868	15%	397.89	345,369	159.16	138,148
Macomb	34,153	9%	383.98	13,114,129	153.59	5,245,652
Manistee	1,661	15%	407.80	677,363	163.12	270,945
Marquette	3,687	13%	374.26	1,379,889	149.70	551,956
Mason	2,037	16%	417.88	851,227	167.15	340,491
Mecosta	2,550	16%	423.84	1,080,784	169.53	432,314
Menominee	1,683	15%	386.34	650,215	154.54	260,086
Midland	4,186	11%	403.71	1,689,925	161.48	675,970
Missaukee	1,010	19%	444.99	449,436	177.99	179,774
Monroe	7,238	10%	404.77	2,929,689	161.91	1,171,876
Montcalm	4,675	16%	404.19	1,889,592	161.68	755,837
Montmorency	854	17%	391.44	334,294	156.58	133,718
Muskegon	13,142	18%	439.67	5,778,081	175.87	2,311,233
Newaygo	2,984	17%	421.85	1,258,787	168.74	503,515
Oakland	44,306	8%	381.39	16,897,824	152.56	6,759,130
Oceana	2,162	18%	443.48	958,805	177.39	383,522
Ogemaw	1,937	19%	415.14	804,126	166.06	321,650
Ontonagon	527	15%	364.02	191,837	145.61	76,735
Osceola	2,125	19%	418.59	889,494	167.43	355,797
Oscoda	604	19%	381.86	230,641	152.74	92,256
Otsego	1,681	14%	435.44	731,976	174.18	292,791
Ottawa	10,009	9%	392.46	3,928,137	156.98	1,571,255
Presque Isle	1,008	15%	405.81	409,053	162.32	163,621
Roscommon	2,194	18%	412.95	906,009	165.18	362,404
Saginaw	16,375	18%	461.25	7,552,989	184.50	3,021,196
Saint Clair	9,296	12%	405.86	3,772,921	162.35	1,509,168
Saint Joseph	4,353	16%	415.10	1,806,941	166.04	722,776
Sanilac	2,982	15%	428.05	1,276,459	171.22	510,584
Schoolcraft	675	17%	412.36	278,343	164.94	111,337
Shiawassee	4,468	13%	401.14	1,792,309	160.46	716,923
Tuscola	3,930	15%	418.69	1,645,456	167.48	658,182
Van Buren	5,774	17%	432.04	2,494,620	172.82	997,848
Washtenaw	11,671	8%	371.61	4,337,049	148.64	1,734,820
Wayne	164,375	20%	469.94	77,247,207	187.98	30,898,883
Wexford	2,658	18%	421.55	1,120,472	168.62	448,189

Source: Calculations by Michigan League for Human Services based on Brookings Institution analysis of Internal Revenue Service data.

Error and Fraud

One concern sometimes voiced in debates over state EITC proposals is that the error rate in the federal EITC has been relatively high. Many who voice such concerns cite a 1999 IRS study that placed the EITC overpayment rate of that year between 27 percent and 31.7 percent, with an overpayment amount at between \$8.5 billion and \$9.9 billion. However, the Center on Budget and Policy Priorities points out that the study had significant methodological flaws that likely resulted in an overstatement of the overpayment rate, particularly in its treatment of non-responders⁵ and in the fact that it counted the total amount paid to claimants who received overpayments rather than counting only the overpaid amount. While even the IRS has acknowledged some of the shortcomings of the study and the fact that the environment has changed significantly since its publication, the study continues to be cited by those who would like to place further procedural requirements on claimants or limit the breadth of the EITC altogether.

Most errors in the past arose from the complex and sometimes contradictory federal tax code rules regarding family relationships, tax filing status and the tax treatment of children (particularly those whose parents are divorced or separated). Many of those rules have subsequently been changed to reduce fraud and errors, and the IRS has implemented measures to validate Social Security numbers listed on tax returns, to alter procedures for obtaining quick turnaround refunds, to crack down on unscrupulous tax preparers, and to improve the targeting of the EITC to low-income families and individuals. Additional compliance measures were passed in 2001 that are estimated to have reduced EITC overpayments by \$2 billion per year.

Because state EITC's are set as a percentage of the federal credit, and tax filers generally must claim the federal credit in order to claim a state

credit, state EITC's are likely to benefit from the enhanced federal EITC compliance efforts. States with EITC's can also introduce their own measures to reduce errors. EITC compliance efforts in New York—the state with the most extensive efforts—include:

- using the social security number reported on the tax form to determine whether two or more taxpayers claimed the same child,
- checking that earnings claimed for the EITC match those on W-2 forms and Schedule C (self-employment) forms, and
- identifying first-time state tax form filers, who are among those most likely to make unintentional errors or to file fraudulently.

States can also identify various categories of EITC claimants found to have high error rates, including those who have filed an erroneous federal claim in the past. Tax returns falling into such categories could then be pulled and subjected to additional verification before EITC is paid. Wisconsin uses such a process as part of its tax compliance efforts.

Summary

A Michigan EITC would provide significant tax relief to a segment of the state's population that has not benefited from recent tax measures to the same extent as other groups. It would supplement low wages and complement welfare-to-work efforts. It would also provide a boost to local economies, many of which have been hurt by the recent economic downturn and loss of jobs. By building on the strengths of the federal EITC and learning from the practices of other states that have enacted EITC's, the lives of thousands of low-income families throughout the state can be improved.

⁵A significant fraction of the families selected for the study did not respond to the IRS when contacted; the low end of the estimate—27 percent—assumed that the overpayments among the non-responders occurred at the same rate as among those who responded, while the high end of the estimate assumed that all of the non-responders were ineligible for every EITC dollar they received. The conclusions of the study do not take into account that many low-income persons for various reasons (intimidation, not understanding the questions, lack of English fluency, etc.) do not respond to such studies, and that there is a possibility that the percentage of non-responders that are eligible for the credit may be much higher than the percentage of responders that are eligible. If this is true, the actual percentage of overpayments would be significantly lower than what the study's conclusion indicates.

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