Department of Legislative Services

Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

House Bill 896 (Delegate Rosenberg, *et al.*)
Ways and Means

Income Tax - Earned Income Tax Credit - Noncustodial Parent

This bill provides that a qualifying noncustodial parent age 18 or older with a child support order can claim an enhanced nonrefundable State earned income credit (EIC). The value of the credit is equal to 50% of the federal EIC for the individual calculated as if the individual had one qualifying child. The tax credit cannot exceed the tax liability in that year. During the tax year, the individual must make, at a minimum, child support payments equal to the amount of current child support payments due for each child support order. Any individual who qualifies for the existing State EIC cannot claim the credit. The Department of Human Resources (DHR) and the Comptroller's Office must jointly adopt regulations to implement the tax credit program.

The bill takes effect July 1, 2009, and applies to tax year 2009 and beyond.

Fiscal Summary

State Effect: General fund revenues decrease by $1.1 million in FY 2010 due to expansion of the State EIC. Future years reflect an increase in the number of claimants and the value of the credit. General fund expenditures increase by $46,600 in FY 2010 for implementation costs at DHR and the Comptroller's Office. Federal fund expenditures increase by $17,800 in FY 2010 for implementation costs at DHR.

($ in millions)	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
GF Revenue	($1.09)	($1.11)	($1.14)	($1.17)	($1.20)
GF Expenditure	$.05	$0	$0	$0	$0
FF Expenditure	$.02	$0	$0	$0	$0
Net Effect	($1.15)	($1.11)	($1.14)	($1.17)	($1.20)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law: Taxpayers can claim a State EIC equal to 50% of the federal credit allowed. The amount of the credit cannot exceed the taxpayer's tax liability in that tax year. Taxpayers may claim a refundable State EIC if the EIC exceeds the individual's State tax liability.

An individual who qualifies for the federal EIC can claim a nonrefundable State EIC equal to 50% of the federal EIC, not to exceed the total pre-credit State income tax liability. In addition, the individual can claim the credit against the county income tax in an amount equal to the lesser of 10 times the county income tax rate multiplied by the federal EIC or the county income tax imposed in the year.

Individuals may also claim a refundable earned income credit equal to the amount, if any, by which 25% the federal EIC exceeds the total pre-credit income tax liability. To the extent provided, the county refundable EIC is the amount by which five times the federal EIC multiplied by the county income tax rate exceeds the county income tax liability. An individual in tax year 2008 can claim a State credit only if he/she meets the eligibility of the federal credit under Section 32 of the Internal Revenue Code as discussed below:

- must have federal adjusted gross income (FAGI) less than $38,646 (more than one qualifying child), and $12,880 (no children). Married couples can earn $3,000 more than these specified limits;
- have a valid Social Security number;
- cannot file under Married Filing Separately;
- must be a U.S. citizen or resident alien for the entire year;
- cannot file Form 2555 (Foreign Earned Income) or Form 2555-EZ (Foreign Earned Income Exclusion);
- must have $2,950 or less investment income; and
- must have earned income – individuals must work and have earned income (disability payments up to minimum retirement ages qualify).

In addition to the qualifications above, individuals without a qualifying child must:

- be at least 25 but under 65 years old;
- not be a dependent or a qualifying child of another person; and

- have lived in the United States for more than half of the year.

Individuals might otherwise qualify for the credit but are prohibited from claiming the credit for specified times if the Internal Revenue Service (IRS) determined that the individual previously claimed the credit fraudulently or through reckless or intentional disregard of EIC rules.

Background: The following is a summary of the federal and State EIC programs.

Federal EIC

The federal EIC began in 1975 as a temporary program to return a portion of the Social Security taxes paid by lower-income taxpayers and was made permanent in 1978. The Tax Reform Act of 1986 increased the maximum benefit of the credit and phase-out levels and indexed the credit to inflation. The next substantive expansion of the credit occurred in the 1990s with the federal Omnibus Budget Reconciliation Acts of 1990 and 1993. Both laws again increased the value of the credit and phase-out levels. The 1990 law provided for different credit amounts for taxpayers with one or two and more children, and the 1993 law expanded the credit to childless taxpayers.

The expansion of the credit in the 1990s is estimated to have tripled the cost of the credit, and the credit is now the largest anti-poverty entitlement program. The federal EIC is generally considered a successful anti-poverty program by researchers. A joint IRS and U.S. Department of Treasury task force estimated that nationwide the EIC lifted 4.3 million individuals, including 2.3 million children, out of poverty in 2000.

State EIC

Maryland's income tax law has provided a nonrefundable State EIC equal to 50% of the federal EIC since 1987. Chapter 5 of 1998 established a refundable EIC for taxpayers who both meet the eligibility standards of the federal credit and have at least one dependent. The value of the initial refundable credit was equal to 10% and increased in two steps to 15% in tax year 2001 and beyond.

Chapter 493 of 1999 altered the calculation of the credit allowed against the county income tax in response to the 1997 tax law establishing flat county income tax rates. The amount of credit allowed against the county income tax is equal to the amount of federal EIC claimed multiplied by 10 times the county income tax rate, not to exceed the county income tax liability for the tax year.

Chapter 510 of 2000 accelerated to tax year 2000 the 15% value of the credit and also authorized counties to provide, by law, a county refundable EIC. While no county has provided a refundable credit that can be claimed with the tax return under the formula provided under State law, Montgomery County's Earned Income Credit program acts as a grant program by matching the State EIC claimed by the taxpayer. Under the program, eligible taxpayers receive a check from the Comptroller, but the grants are paid for by Montgomery County.

Chapter 581 of 2001 phased in an additional 5% increase in the value of the credit, with a three-step increase of the credit increasing its value to 20% beginning in tax year 2004. Chapter 3 of the 2007 special session increased the value of the credit to 25% and expanded eligibility to include childless adults.

In tax year 2007, 252,741 tax returns claimed approximately $73.8 million in State EICs, and 214,569 claimed approximately $97.7 million in State refundable EICs. The amount of refundable State credits that will be claimed in tax year 2009 will be significantly higher due to enhancement in the value as enacted in the 2007 special session and the recent temporary expansion of the federal credit for certain individuals. In tax year 2006, the last year of available data, 353,488 State taxpayers claimed approximately $1.2 billion in federal EIC credits.

State Revenues: The bill expands eligibility of the State EIC to noncustodial parents beginning in tax year 2009. As a result, general fund revenues will decrease by $1.1 million in fiscal 2010. This estimate is based on the following facts and assumptions:

- According to DHR, there are approximately 112,000 noncustodial parents who during the tax year pay child support payments equal to the amount of current child support payments due for each child support order.
- Approximately 6% of these individuals receive public assistance and are assumed to not file an income tax return.
- Slightly more than 10% of noncustodial parents are estimated to meet the eligibility requirements of the earned income credit.
- Based on average tax liabilities and the value of the federal EIC, each individual claims on average $225.
- Future year revenue losses increase by 2.5% annually.
- 30% of individuals already qualify for the State EIC or poverty level credit.
- One-third of obligors are not residents.

State Expenditures: DHR will incur a one-time computer system programming cost of $26,950 in fiscal 2010 in order to implement the bill. Of this amount, $9,163 is general funds and $17,787 is federal funds.

The Comptroller's Office will incur a one-time expenditure increase of $37,400 in fiscal 2010 to add the credit to the personal income tax form. This amount includes data processing changes to the SMART income tax return processing and imaging systems and systems testing.

In total, general fund expenditures will increase by $46,563 in fiscal 2010 and federal fund expenditures will increase by $17,787.

Additional Information

Prior Introductions: HB 1331 of 2008 and HB 534 of 2007 received a hearing in the House Ways and Means Committee but no further action was taken on either bill.

Cross File: None.

Information Source(s): Department of Human Resources, Comptroller's Office, Department of Legislative Services

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