

Department of Legislative Services
Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 573
(Delegate Platt, *et al.*)
Ways and Means

Income Tax - Earned Income Tax Credit - Eligibility Awareness Campaign

This bill establishes an Earned Income Tax Credit Eligibility Awareness Campaign in the Department of Human Services (DHS). The purpose of the program is to encourage eligible individuals to claim the federal and State earned income tax credits. The Governor must include at least \$100,000 in the State budget to fund the program beginning in fiscal 2020. **The bill takes effect July 1, 2018, and applies to tax years 2018 and beyond.**

Fiscal Summary

State Effect: General fund expenditures increase by \$55,000 in FY 2019, which reflects implementation costs at the Comptroller's Office. Future year expenditures reflect ongoing mandated appropriations to DHS. Revenues are not directly impacted. **This bill establishes a mandated appropriation beginning in FY 2020.**

(in dollars)	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
Revenues	\$0	\$0	\$0	\$0	\$0
GF Expenditure	55,000	100,000	100,000	100,000	100,000
Net Effect	(\$55,000)	(\$100,000)	(\$100,000)	(\$100,000)	(\$100,000)

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

Local Effect: None.

Small Business Effect: None.

Analysis

Bill Summary: The Comptroller must include (1) a checkoff on the individual income tax return form that authorizes the disclosure of specified taxpayer information to DHS including income and whether the taxpayer claimed the federal earned income tax credit (EITC) and (2) a description of the purposes for which the disclosed information may be used. If the taxpayer authorizes the disclosure of the information, the Comptroller may provide the information to DHS.

DHS, in consultation with the Comptroller, must implement and administer the awareness campaign and:

- administer the fund established by the bill;
- inform individuals who apply for or receive public benefits about the federal and State earned income tax credits;
- based on the information provided by the Comptroller, identify and notify by mail eligible individuals who fail to claim the earned income tax credits;
- partner with private entities to increase general awareness of the credits;
- adopt regulations to implement the program; and
- report annually to the General Assembly on program implementation and administration.

The bill establishes a special nonlapsing fund that consists of money appropriated to the fund, interest earnings, and any other money accepted for the benefit of the fund. Money expended from the fund is supplemental to and is not intended to replace funding that would otherwise be appropriated to DHS. DHS may use the fund to award grants to private entities that partner with the agency and pay for necessary notification costs.

Current Law: First enacted in 1975, the federal earned income tax credit is a refundable tax credit offered to low-income workers. The federal credit has expanded significantly over time and is now one of the largest federal antipoverty programs.

Maryland offers a nonrefundable credit, which is equal to the lesser of 50% of the federal credit or the State income tax liability in the taxable year. If the nonrefundable credit reduces a taxpayer's liability to zero, the taxpayer is eligible to claim a refundable credit equal to 28% of the federal credit in tax year 2018, minus any precredit State tax liability. The Comptroller's Office administers the State tax credit.

Background:

Earned Income Tax Credit Activity and Participation

Fifteen percent of tax returns, or a little more than 1 in 7 returns overall, claimed the State credit in tax year 2012, with the incidence of the credit widespread across urban, suburban, and rural areas. The two jurisdictions with the highest utilization of the credit, with a little more than 1 in 4 returns claiming the credit, are Baltimore City (population 622,100) and Somerset County (population 26,500). In addition, residents are 20% more likely to claim the credit in Prince George's County, Western Maryland, and five of the nine Eastern Shore counties. Residents are less likely to claim the credit in Montgomery, Kent, Talbot, and Queen Anne's counties and Southern and Central Maryland. Even within high-income counties with the lowest percentage of claims (Carroll and Howard counties), the credit is claimed by 1 in 13 tax returns.

The participation rate is the percent of the eligible population that claims the earned income tax credit. Nationally, approximately 79% of all eligible taxpayers claimed the federal credit in tax year 2010; in Maryland, the federal credit participation rate was slightly lower at 76.4%. Historically, one in four eligible taxpayers have failed to claim the federal credit.

The Internal Revenue Service (IRS) found that households who are eligible but do not file a tax return account for approximately two-thirds of nonparticipants. Additionally, research indicates that participation is significantly lower for households that are not required to file a return (35% compared with 90% for those taxpayers who are required). The IRS and the U.S. Government Accountability Office found that those eligible for a higher credit are more likely to claim the credit.

Research has also found that receiving income from Social Security and public assistance, having a larger family, and being unmarried, male, or Hispanic were significantly correlated with nonparticipation. The IRS reports that the people who fail to claim the EITC typically include those (1) living in nontraditional homes, such as a grandparent raising a grandchild; (2) whose earnings declined or whose marital or parental status changed; (3) without children; (4) with limited English skills; (5) living in rural areas; (6) with earnings below the filing threshold; and (7) who have disabilities or are raising children with disabilities.

The Department of Legislative Services (DLS) estimates that an additional 131,300 Maryland households could have claimed \$81.3 million in federal credits in tax year 2012 but did not. An estimated 95% of those claiming the federal credit claim the State credit, and the estimated amount of potential State credit left unclaimed is slightly higher at 10% of the total amount actually received. As such, an additional 150,800 households could have also claimed a total of \$24.5 million in State credits.

Nonparticipants were eligible for an average federal credit of \$619 and State credits of \$162. A 1% increase in the participation rate would provide an additional \$3.4 million in federal credits and \$0.9 million in State credits to an additional 5,600 Maryland households.

Maryland's participation rate ranks thirty-eighth among the 50 states and the District of Columbia. Mississippi has the highest participation rate (85.2%) while Oregon has the lowest (71.0%). With the exception of the District of Columbia and New Jersey, Maryland's surrounding states have higher participation rates.

The participation rate of the federal EITC has generally been higher than most other social safety net programs. The EITC participation rate (79.0%) is comparable to the Supplemental Nutrition Assistance Program (SNAP) participation rate (78.9%). In Maryland, the EITC participation rate in tax year 2010 was 76.4%, slightly below the national average, while the Maryland SNAP participation rate in fiscal 2011 was 81.0%, slightly above the national average. Temporary Assistance for Needy Families and Social Security Income had lower federal participation rates of 32% and 65%, respectively.

DHS departmental goals, objectives, and performance measures typically include achieving program workforce participation rates and maintaining error levels below certain percentages. Due to the nature of how the federal and State credits are calculated and claimed, there is no Maryland agency charged by statute to promote public awareness of the credit or its eligibility requirements.

Department of Legislative Services Evaluation

Pursuant to the Tax Credit Evaluation Act of 2012, DLS evaluated the State earned income credit and made several recommendations in a final report issued in September 2015. The report concluded that while there is general consensus that earned income tax credits are effective in raising low-income households out of poverty, it is not without issues. Credit effectiveness is limited by high rates of improper payments, the use of paid tax preparers that charge high-cost products which reduce the value of the credit, and participation rates that could be improved. Additionally, the ability of the credits to reduce concentrated poverty and deep poverty is limited given the work component of the credit.

Based on the information and analysis provided in the report, DLS recommended several changes to improve the tax credit. DLS recommended that the General Assembly designate DHS, in consultation with the Office of the Comptroller, to promote the credit and gather information regarding participation rates and credit effectiveness. DLS also recommended that State earned income credit goals, objectives, and performance measures (*e.g.*, obtaining a certain State credit participation rate) be integrated into DHS's objectives and budget measures.

The DLS evaluation of the earned income credit can be found [here](#).

State Expenditures: General fund expenditures increase by \$55,000 in fiscal 2019 and by about \$100,000 annually beginning in fiscal 2020, as discussed below.

Department of Human Services

The Governor must include at least \$100,000 in the State budget to fund the program beginning in fiscal 2020. Assuming the program is funded at this level, general fund expenditures will increase by \$100,000 annually beginning in fiscal 2020. However, there is no limit on the amount that can be appropriated to the fund. To the extent that the Governor provides more money to the fund in any year, the increase in general fund expenditures will be greater.

The bill applies beginning with tax year 2018 tax returns, which will be generally processed by December 2019. It is assumed that any implementation costs incurred in fiscal 2019 are minimal and absorbable within existing budgeted resources.

Comptroller's Office

The Comptroller's Office reports that it will incur a general fund expenditure increase of \$55,000 in fiscal 2019 to add the checkoff and required information to the personal income tax forms and instructions. This includes data processing changes to the SMART income tax return processing and imaging systems and systems testing. General fund expenditures increase minimally beginning in fiscal 2020 due to additional printing costs.

Additional Information

Prior Introductions: HB 762 of 2017 received a favorable with amendments report from the House Ways and Means Committee, passed the House, and received a hearing in the Senate Budget and Taxation Committee, but no further action was taken.

Cross File: None.

Information Source(s): Comptroller's Office; Internal Revenue Service; U.S. Department of Agriculture; U.S. Department of Health and Human Services; U.S. Government Accountability Office; Department of Legislative Services

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