

**MICHIGAN EARNED INCOME
TAX CREDIT
Tax Year 2012**



**Office of Revenue and Tax Analysis
Michigan Department of Treasury
March 2014**

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Acknowledgments

Scott Darragh prepared this statistical update under the direction of Howard Heideman, Director of the Tax Analysis Division, Office of Revenue and Tax Analysis, Michigan Department of Treasury.

Introduction

Public Act 372 of 2006 created the Michigan earned income tax credit (EITC). For the 2008 tax year, an eligible taxpayer could claim a credit against the Michigan income tax equal to 10 percent of the federal earned income tax credit for which the taxpayer is eligible. By using the federal eligibility standards for the Michigan credit the credit “piggy-backs” on the federal credit. Beginning with the 2009 tax year, the Michigan credit increased to 20 percent of the federal credit. If the Michigan EITC exceeds the taxpayer’s income tax for the year the excess credit is paid as a tax refund. Public Act 38 of 2011 reduced the Michigan EITC to 6 percent of the federal credit, effective for tax years that begin after December 31, 2011. Tax year 2012 was the first tax year with the credit equal to 6 percent of the federal EITC amount.

The purpose of this report is to present statistical data on the Michigan EITC for 2012, the fifth year the credit was available for Michigan taxpayers. The data presented here are based on approximately 772,270 tax returns that claimed and received an EITC for 2012. Statistics for the Michigan EITC are presented for filing status, processing date, income level, children claimed as dependents, and the impact of the EITC on poverty status.

Background on the Federal EITC

The federal EITC was established in 1975 as a way to offset the impact of the Social Security tax on low-income, working families. After several expansions, the EITC is now the largest cash benefit program in the country. More than 19 percent of all tax returns filed nationally claimed an EITC for 2011, the latest year for which complete data are available. In Michigan, 18.4 percent of all returns filed claim a federal EITC. The federal EITC for tax years 2009 through 2017 has been increased for some married couples and for taxpayers with three or more qualifying children. For 2012, the credit may be as large as \$5,891 for a family with three or more qualifying children.

The EITC has three distinct ranges, depending upon an eligible taxpayer’s income. Charts 1 and 2 depict the 2012 EITC for unmarried filers and couples filing a joint return, respectively. Income, for purposes of the EITC, means either the taxpayer’s adjusted gross income or earned income from wages, salaries, or business income, whichever produces the smallest credit. The EITC initially rises with additional earned income, effectively acting as a subsidy for work. The subsidy rates are 7.65 percent for recipients without qualifying children, 34 percent for recipients with one qualifying child, 40 percent for recipients with two qualifying children, and 45 percent for recipients with three or more qualifying children. The income subsidy range ends at \$6,210 for recipients without qualifying children, resulting in a maximum credit of \$475 for 2012. For recipients with one qualifying child, the subsidy range ends at \$9,320 resulting in a maximum credit of \$3,169. For recipients with two and three or more qualifying children, the subsidy range ends at \$13,090 resulting in maximum credits of \$5,236 and \$5,891, respectively.

The second range is often referred to as the cash-grant range, since the EITC amount is unchanged even if a recipient’s income changes within the range. The cash-grant range is between \$6,070 and \$7,770 for recipients without qualifying children who are not married and

filing a joint return, between \$9,320 and \$17,090 for recipients with one qualifying child and not filing a joint return, and between \$13,090 and \$17,090 for recipients with two and three or more qualifying children and not filing a joint return. In order to reduce the marriage penalties associated with the EITC, the cash-grant range for 2012 is extended by \$5,210 for all recipients who are married and filing a joint return.

The EITC is phased out in the third range, so additional income will result in a smaller EITC amount. The phase-out range effectively taxes additional earned income by reducing the credit as the recipient's income rises. For recipients without qualifying children, the credit is reduced by 7.65 percent of any income over \$7,770, and the credit is eliminated for incomes over \$13,980 for taxpayers whose filing status is single or head of household. The phase out range begins at \$12,980 and is completed at \$19,190 for those filing a joint return without qualifying children. The phase out begins at \$17,090 and is complete at \$36,920 for unmarried recipients with one qualifying child. As a result, the credit is reduced by approximately 16 percent of any income above \$17,090. The phase out range begins at \$22,300 and is completed at \$42,130 for those with one qualifying child who file a joint return. For unmarried recipients with two qualifying children and those with three or more qualifying children the phase out begins at \$17,090. For recipients with two qualifying children the phase out is complete at \$41,952, while the phase out is complete at \$45,060 for recipients with three or more qualifying children. As a result, the credit is reduced by approximately 21 percent of any income above \$17,090. The phase out range begins at \$22,300 and is completed at \$47,162 for those joint filers with two qualifying children and at \$50,270 for joint filers with three or more qualifying children.

2012 Michigan EITC

For tax year 2012, almost 772,300 taxpayers received the Michigan EITC. Just under \$106.4 million in total credits were claimed, with the average credit equal to \$138. The average taxpayer claiming an EITC had a federal adjusted gross income (AGI) equal to \$17,397. The average was \$17,778 for those with AGI greater than zero. For the approximately 766,500 EITC recipients with AGI greater than zero, the Michigan EITC averaged approximately 0.8 percent of AGI, lower than the average of 2.6 percent for 2011.

Table 1 reports 2012 EITC recipients by AGI. The heaviest concentration of EITC returns occurs between \$5,000 and \$15,000 in AGI, with just under 40 percent of all EITC returns reporting an AGI in this range. The average credit is highest for recipients between \$15,000 and \$20,000, with the average credit for this group equal to \$232 for 2012. This income group is dominated by taxpayers with qualifying children and the unmarried taxpayers with qualifying children are beginning the phase-out range once income reaches \$17,090.

Beginning with tax year 2012, Michigan no longer has a separate deduction for children age 18 and under. In order to estimate the number of EITC returns with qualifying children, the number of federal exemptions claimed on the Michigan return was reduced by the number of taxpayers and spouses represented on the return. For example, a return filed as single with three federal exemptions would be assumed to have two qualifying children, while a joint return with three federal exemptions would be assumed to have one qualifying child. Table 2 shows the

distribution of the Michigan EITC by the number of estimated qualifying children. Approximately 25 percent of the credits are claimed by taxpayers who do not claim a child exemption, but these credits are small and reflect the smaller federal credit for those without a qualifying child. The average credit for taxpayers who do not claim a child exemption is \$20, less than 15 percent of the overall average credit. The average credit for those claiming two or more estimated exemptions for children is \$213.

The vast majority of EITC recipients are unmarried, with more than 70 percent reporting single as their filing status. Table 3 shows the distribution of the Michigan EITC by filing status. The average credit for single filers is approximately 14 percent smaller than the average for married filers. While the expanded federal credit range for married claimants may explain some of the difference in average credits, the average AGI of married claimants is also significantly higher than the average AGI of single filers.

Over 384,300 (49.8 percent) of EITC recipients also received a homestead property tax credit (HPTC), the longstanding Michigan credit designed to provide tax relief to Michigan residents with property taxes that exceed a percentage of their total income specified in statute, typically 3.5 percent of income. Renters are eligible for the credit if rent exceeds 17.5 percent of total income. For those taxpayers who received both credits, the average EITC was \$157 while the average HPTC was \$464. Total payments to taxpayers who received both credits were \$238.6 million, \$60.3 million in Michigan EITC and \$178.4 million in HPTC payments.

EITC claimants on average file their returns earlier than the typical Michigan taxpayer. The distribution of EITC returns by processing date is presented in Table 4, and two key facts are observable. First, EITC returns are filed and processed very early in the processing season with 54 percent of the credits processed prior to the end of February while approximately 31 percent of all individual income tax returns processed during 2013 were completed by the end of February. Second, the average EITC amount is higher on returns filed early compared to those filed later in the season. The average EITC amount in January and early February (\$178) is much higher than the average credit on returns processed in March and April (\$110). The early filing of EITC returns no doubt reflects the expectation on the part of the taxpayer for a substantial refund.

The structure of the EITC, at both the federal and state levels, targets the largest benefits to working households near the poverty level. For example, the maximum federal EITC for a family of three with two qualifying children is available at incomes between \$13,090 and \$17,090. This income level approximates what a full-time worker would earn for the year if they worked at or near the federal or Michigan minimum wages. The poverty guideline from the U.S. Department of Health and Human Services for 2012 for a family of three was \$19,090. The additional resources provided through the federal and Michigan EITCs would have moved a family of three with earnings roughly equivalent to full-time employment at the minimum wage from below the poverty guideline to above the poverty guideline. The maximum federal EITC for two qualifying children was \$5,236 for tax year 2012, and the Michigan EITC would be \$5,236 x 6 percent or \$314 for a combined total of \$5,550. While not every family who qualifies for a significant EITC payment is lifted out of poverty, the combined benefits of the federal and Michigan EITCs can significantly improve the financial condition of the working poor.

To measure the impact of the federal and Michigan EITCs on the poverty status of Michigan claimants, each claimant's AGI and Michigan EITC were used to construct a ratio of income to the poverty guideline based on family size. Each taxpayer receiving a Michigan EITC reports AGI, claims federal exemptions equal to the number of taxpayers and dependents in the home, and claims a Michigan EITC¹. Based on the number of federal exemptions a poverty guideline amount can be assigned to the tax return. Since the Michigan EITC is equal to 6 percent of the federal EITC, the federal EITC amount can be imputed from the Michigan EITC amount. Using this information, a comparison of income before and after the EITC can be constructed².

A commonly used measure of poverty status is the ratio of income to a standard of poverty. A ratio of less than 1 means the household's income is below the poverty standard and the household is considered to be in poverty. A ratio of 1 means the household is right at the poverty standard, and a ratio above 1 means the household has an income above the poverty standard. To evaluate the impact of the Michigan and federal EITCs on the poverty status of Michigan claimants, three ratios are computed for each claimant. The first ratio is AGI to the poverty guideline. This ratio will look at the poverty status of the claimant's family ignoring the impact of the EITC. While AGI is the most common measure of income used for tax purposes, it is not necessarily the most complete measure. The U.S. Bureau of the Census uses cash income when calculating the poverty statistics, which includes all payments of cash received by the household including government cash assistance, gifts, and other transfer payments such as Social Security and Supplemental Security Income. For the entire population, the difference between AGI and cash income would be significant and using AGI instead of cash income would alter the measured poverty rate somewhat. However, many low-income workers are too young for Social Security benefits and do not receive other cash assistance, so that AGI and cash income as measured by the Census Bureau are very similar.

The distribution of returns by the ratio of AGI to the poverty guideline is shown in the second column of Table 5. For 2012, approximately 135,090 returns (17.6 percent) reported AGI of no more than ½ of the poverty guidelines, a ratio of 0.5 or less. A total of approximately 434,710 returns (56.7 percent) reported AGI at or below the poverty guidelines. Based on AGI alone, the families represented by these returns would be in poverty. Approximately 194,030 returns reported AGI above the poverty guidelines but no more than 1.5 times the poverty guidelines. For a family of three, this would be AGI between \$19,090 and \$28,635. The remaining 137,760 returns reported AGI of more than 1.5 times the poverty guidelines.

The inclusion of the EITC will increase every claimant's ratio of income to the poverty guideline, but an EITC of several thousands of dollars will raise the ratio by 0.1 to 0.3, depending on family size. When the federal EITC is included along with AGI, approximately 345,760 returns are below the poverty guidelines, a decline of 20.5 percent compared to using AGI alone. The third column of Table 5 has the distribution of returns including the federal

¹ The number of federal exemptions will approximate the number of people living in the household well, but there are situations where individuals either living in the household are not claimed as dependents (even if they are qualifying children) or living in another household are claimed as dependents. For example, the exemption for a child may be assigned to a non-custodial parent as part of a divorce or separation agreement.

² Returns with AGI < 0 were excluded. This excluded a total of 5,770 returns (rounded to the nearest 10 returns).

EITC. The inclusion of the federal EITC results in a net movement of approximately 101,340 returns from below to above 0.75 times the poverty guidelines, a decline of 34.8 percent in returns well below the poverty guidelines (≤ 0.75). The fourth column of Table 5 has the net change for each income division once the federal EITC is included. Each income division above 0.75 times the poverty guidelines sees a net increase in the number of returns within the division. This generally occurs because returns in the next lower category prior to the inclusion of the federal EITC move one-step higher as a result of the federal EITC. The approximately 8,310 additional returns that have income greater than 2.0 times the poverty guidelines with the federal EITC included would generally have had a ratio of between 1.5 times and 2.0 times the poverty guidelines without the federal EITC, and not have been at or below poverty. The movement in Table 5 will generally reflect many returns moving one income category.

The Michigan EITC also raises the income of recipients, although by a smaller amount than the federal EITC. The Michigan credit raises a recipient's ratio of income to poverty guideline of 0.1 or less for all but the families with the lowest incomes, so there should be less movement between income divisions as a result of the Michigan credit. When the Michigan EITC is included along with AGI and the federal credit the number of returns below the poverty guidelines falls to 338,960, a drop of 6,800 returns from AGI and the federal credit alone. The combined impact of the federal and Michigan EITCs, done by comparing the fifth column to the second column in Table 5, was to move 95,750 families above the poverty guidelines for 2012. This represents a decline of 22.0 percent compared to AGI alone. These calculations would imply that the combined impact of the Michigan and federal EITCs is to move almost $\frac{1}{4}$ of the working poor above the poverty guidelines.

As noted earlier, the impact of the combined benefit from the federal and Michigan EITCs on families near the poverty guidelines can be very significant, raising disposable income by a third or more³. However, even families that have incomes somewhat above the poverty guidelines would see significant increases in disposable incomes⁴. The additional income provided by the EITCs could provide working families with additional options for housing, child care, or transportation so that the family can remain in the labor force and take steps toward additional self-sufficiency.

If you have questions on this report, please contact Scott Darragh at (517) 241-2148.

³ Note that a married-couple family with two qualifying children and an AGI of \$16,300 would have received a federal EITC of \$5,236 and a Michigan EITC of \$314. Combined with an estimated federal and state tax liability of \$975 (including Social Security and Medicare), the family's disposable income would be increased by 36.2 percent by the combined EITCs. This calculation does not include any refundable portion of the federal Child Tax Credit.

⁴ A single parent with two qualifying children and an AGI of \$30,000 would have received a federal EITC of \$2,512 and a Michigan EITC of \$151. The combined EITCs of \$2,663 represent 8.9 percent of AGI.

Chart 1
Federal EITC 2012 – Unmarried Filers

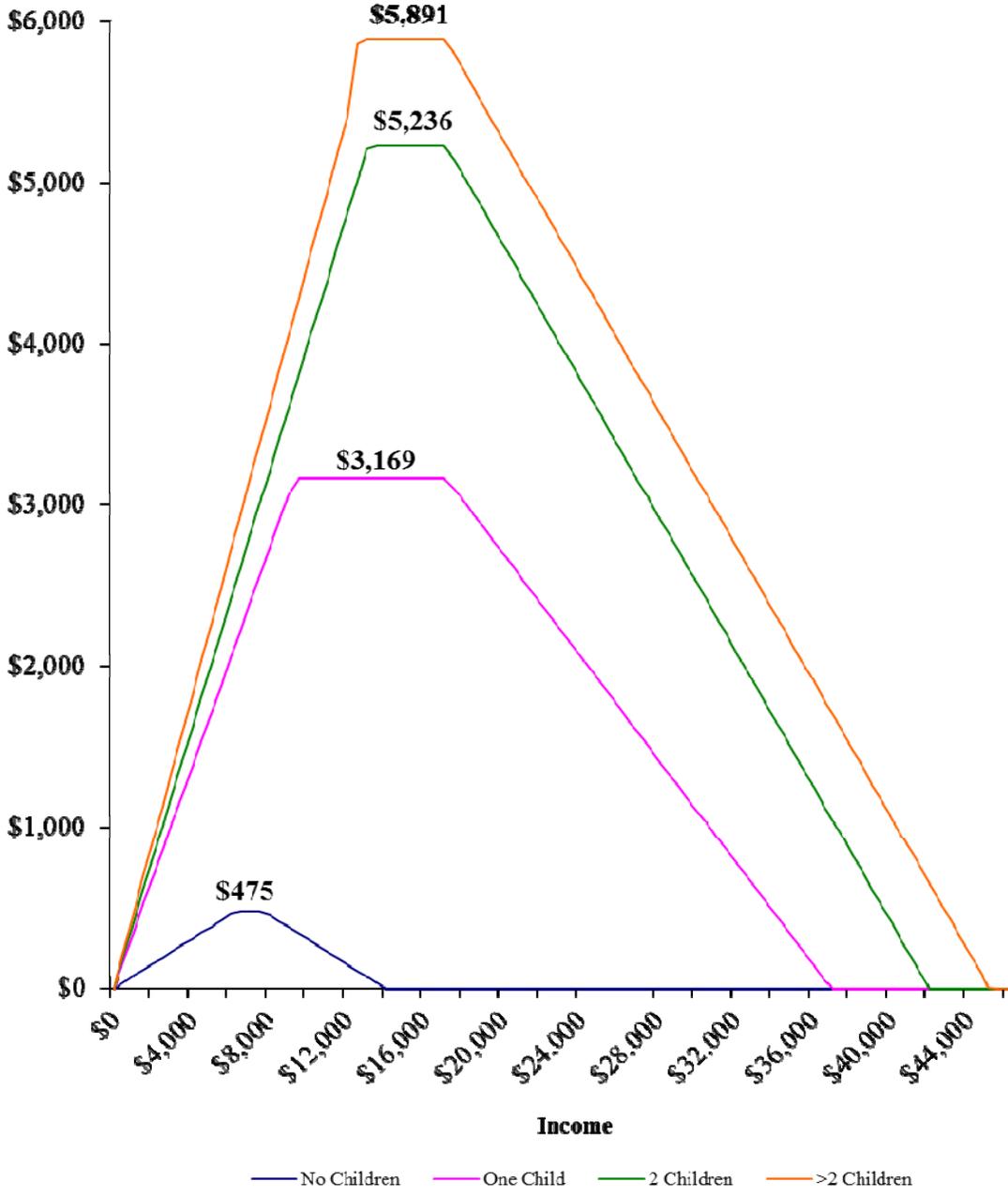


Chart 2
Federal EITC 2012 – Married Filing Jointly

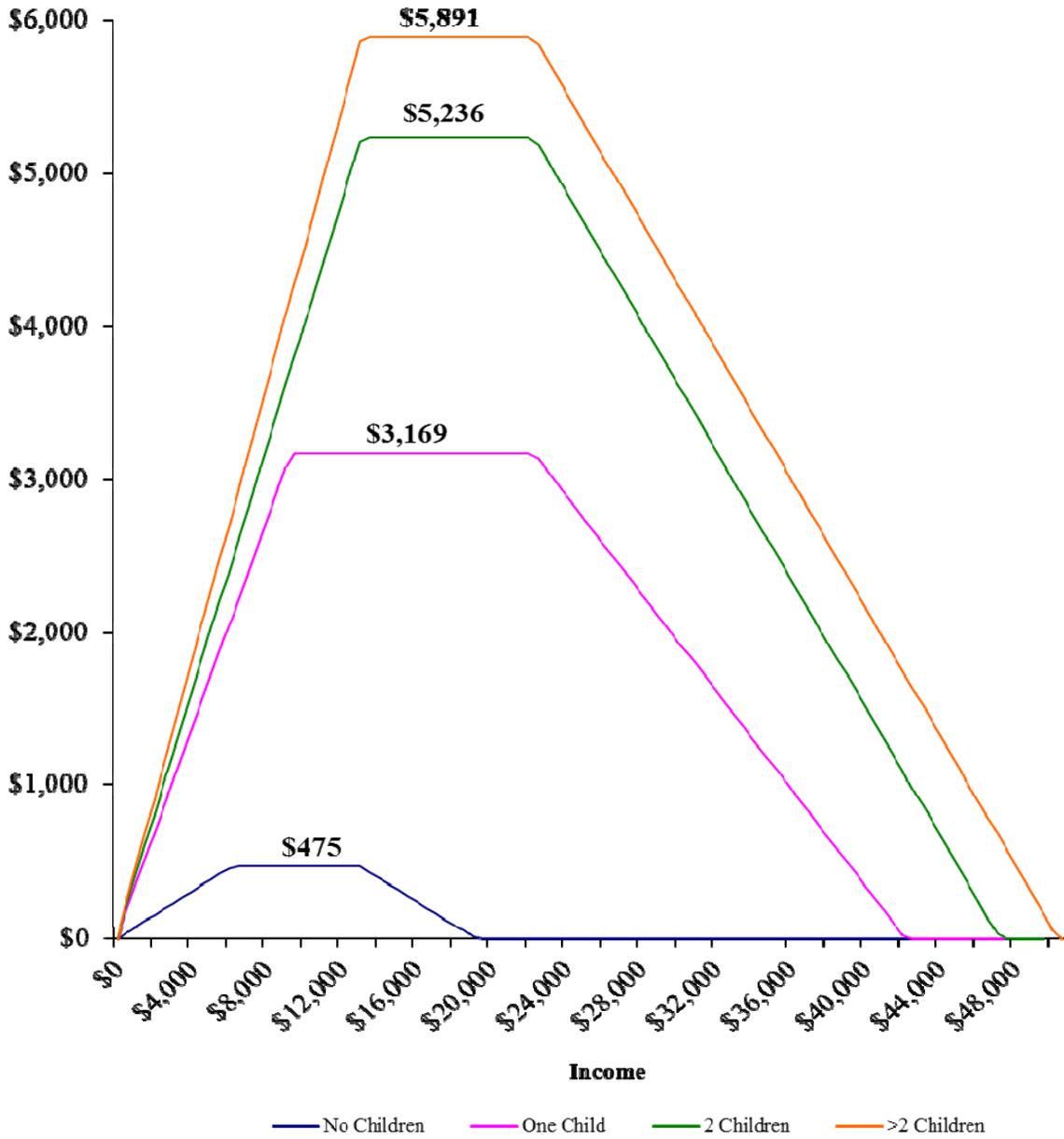


Table 1
EITC Recipients by AGI
Tax Year 2012

<u>AGI Range</u>	<u>Count</u>	<u>Average AGI</u>	<u>Average MI EITC</u>	<u>Total MI EITC (millions)</u>
Less than or = \$0	5,770	-\$33,219	\$60	\$0.3
\$1 - \$5,000	75,370	\$2,828	\$32	\$2.4
\$5,001 - \$10,000	141,660	\$7,822	\$95	\$13.5
\$10,001 - \$15,000	166,090	\$12,394	\$159	\$26.4
\$15,001 - \$20,000	107,290	\$17,320	\$232	\$24.8
\$20,001 - \$25,000	79,010	\$22,442	\$211	\$16.7
\$25,001 - \$30,000	67,540	\$27,434	\$162	\$11.0
More than \$30,000	<u>129,540</u>	\$36,768	\$87	<u>\$11.2</u>
Total	772,270	\$17,397	\$138	\$106.4

Note: Counts are rounded to the nearest 10.

Table 2
EITC Recipients by Estimated Number of Children
Tax Year 2012

<u>Number of Child Exemptions Reported</u>	<u>Count</u>	<u>Average AGI</u>	<u>Average MI EITC</u>	<u>Total MI EITC (millions)</u>	<u>Total Children Reported</u>
0	193,170	\$7,694	\$20	\$3.8	0
1	259,500	\$18,204	\$133	\$34.5	259,500
2	197,750	\$21,719	\$204	\$40.3	395,500
3	88,740	\$23,440	\$231	\$20.5	266,220
4 or more	<u>33,120</u>	\$25,670	\$220	<u>\$7.3</u>	<u>146,010</u>
Total	772,280	\$17,397	\$138	\$106.4	1,067,230

Note: Counts are rounded to the nearest 10.

Table 3
EITC Recipients by Filing Status
Tax Year 2012

<u>Filing Status</u>	<u>Count</u>	<u>Average AGI</u>	<u>Average MI EITC</u>	<u>Total MI EITC (millions)</u>
Single	568,010	\$14,912	\$132	\$75.2
Married filing joint	204,070	\$24,314	\$153	\$31.2
Married filing separate	200	\$17,290	\$123	\$0.0
Total	772,280	\$17,397	\$138	\$106.4

Note: Counts are rounded to the nearest 10. The amount of EITC claimed on returns that do not indicate a filing status was under \$50,000.

Table 4
EITC Recipients by Processing Date
Tax Year 2012

<u>Return Processed</u>	<u>Percent of Total</u>	<u>Cumulative Percent of Total</u>	<u>Average MI EITC</u>	<u>Total MI EITC (millions)</u>
January	2.6%	2.6%	\$177	\$3.5
Feb. 1 - Feb. 14	29.5%	32.1%	\$178	\$39.2
Feb. 15 - Feb. 28	22.2%	54.3%	\$151	\$25.1
March	22.8%	77.1%	\$126	\$21.6
April	14.3%	91.4%	\$92	\$9.9
After April	8.6%	100.0%	\$111	\$7.1
Total	100.0%		\$138	\$106.4

Table 5
Impact of Federal and Michigan EITC on Poverty Status
Tax Year 2012

<u>Ratio of Income to Poverty Guidelines</u>	<u>AGI Alone Count</u>	<u>AGI plus Federal EITC</u>	<u>Change from federal EITC</u>	<u>AGI plus Federal and Michigan EITC</u>	<u>Additional Change with Michigan EITC</u>
No more than 0.5	135,090	97,230	-37,860	95,730	-1,500
>0.50 and <= 0.75	156,250	92,770	-63,480	90,850	-1,920
>0.75 and <=1.0	143,370	155,760	12,390	152,380	-3,380
>1.0 and <=1.25	123,230	149,740	26,510	151,880	2,140
>1.25 and <=1.50	70,800	93,890	23,090	95,460	1,570
>1.50 and <=2.0	104,360	135,410	31,050	137,850	2,440
Greater than 2.0	<u>33,400</u>	41,710	8,310	42,350	640
Total	766,500				
Total Below Poverty	434,710	345,760		338,960	
Total Above Poverty	331,790	420,750		427,540	
Total Moving Above Poverty		88,960		6,790	

Note: Counts are rounded to the nearest 10.