

REPORT OF THE CHIEF LEGISLATIVE ANALYST

October 25, 2010

To: Honorable Members of the Jobs
and Business Development Committee

From: Gerry F. Miller *KEK*
Chief Legislative Analyst

Council File No.: 09-2750
Assignment No.: 10-01-0029

Status Report -- Improving Receipt of the Earned Income Tax Credit (EITC) in Los Angeles

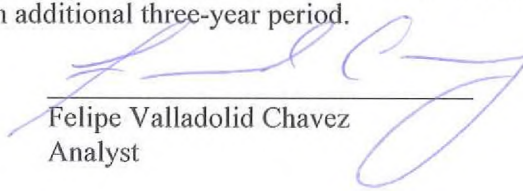
SUMMARY

On December 12, 2009, the Council instructed our Office to report on the process for developing a Memorandum of Understanding (MOU), or other agreement, with the Internal Revenue Service (IRS) and/or California Franchise Tax Board, to implement an Earned Income Tax Credit (EITC) Program similar to the program in the City of New York (NYC) (C.F. 09-2750) (Alarcón-Wesson). According to the IRS, because the City of Los Angeles does not collect a Local Income Tax, the City is unable to establish a data-sharing relationship with the IRS that would allow for the development of an EITC Program similar to the NYC model. The attachment contained in this status report describes an alternative EITC effort by the IRS, and other partners, which resulted from initial discussions at the Jobs and Business Development Committee meeting of November 17, 2009 and a recommendation for implementation. Additionally, the status report describes San Francisco's Working Families Credit (WFC) and provides a recommendation to explore possible implementation of a similar program in Los Angeles. Lastly, we include a recommendation urging the United States Congress to extend the EITC Credit, currently provided through American Recovery and Reinvestment Act (ARRA) funds, to workers with three or more children for an additional three-year period.

RECOMMENDATIONS

That the City Council:

1. Instruct the Community Development Department, with the assistance of the Housing Department, Community Redevelopment Agency, Transportation, Personnel, and Council Offices, to work with Internal Revenue Service (IRS), to develop a marketing campaign to ensure that the over 7,000 Earned Income Tax Credit (EITC) eligible individuals and families in the City of Los Angeles are notified of a possible IRS reimbursement.
2. Instruct the Community Development Department, with the assistance of the City Administrative Officer and the Chief Legislative Analyst, to explore the possibility of implementing a local EITC program similar to the San Francisco Working Families Credit Program and report back in 90 days.
3. Instruct the Office of the Chief Legislative Analyst to prepare a Resolution urging the United States Congress to extend the EITC increase, currently provided through American Recovery and Reinvestment Act (ARRA) funds, to working families and individuals with three or more qualifying children, for an additional three-year period.


Felipe Valladolid Chavez
Analyst

Attachments: 1) Background, 2) Motion (Alarcón-Wesson)

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BACKGROUND**Earned Income Tax Credit (EITC)**

The EITC is a refundable federal income tax credit for low to moderate income working individuals and families. Congress originally approved the tax credit legislation in 1975, in part, to offset the burden of social security taxes on working individuals and to provide an incentive to work. When EITC exceeds the amount of taxes owed, it results in a tax refund to those who claim and qualify for the credit. Benefit amounts change based on an individual's yearly earnings. Table 1 below provides the income limits for Tax Year 2009. In Tax Year 2009, the maximum EITC Credit for an individual filing single or married with three or more qualifying children was \$5,657, although reaching this amount is not likely given various qualifying factors. The actual EITC Credit per individual is determined by factors such as marital status, income limits, and family size. Tables 2 and 3 describe the specific requirements that potential recipients of EITC Credit would have to meet. All EITC filers must also meet the following requirements:

- Have a valid Social Security Number.
- Filing status cannot be "Married Filing Separately."
- Be U.S. Citizen or legal resident all year.
- Investment income must be less than \$3,100
- Must have earned income.

2009 Tax Year Income Limits

To qualify for the EITC Credit, Earned Income and Adjusted Gross Income must each be less than the specified amounts shown on Table 1¹.

Table 1- Income Limits

Earned Income and Adjusted Gross Income Limits		Number of Qualifying Children
Filing Single	Married Filing Jointly	
\$43,279	\$48,279	3 or more
\$40,295	\$45,295	2
\$35,463	\$40,463	1
\$13,440	\$18,440	0

Source: IRS.gov

Table 2- Individuals With Qualifying Children

RELATIONSHIP TEST	AGE TEST	RESIDENCY TEST	JOINT RETURN
<ul style="list-style-type: none"> - Son, daughter, stepchild, foster child, or a descendant of any of them (i.e. grandchild) - Brother, Sister, and any descendant. 	<ul style="list-style-type: none"> - Under 19 and younger than individual filing. - Under 24, student, and younger than individual filing. - Permanently disabled at any age. 	<ul style="list-style-type: none"> - Child must have lived in the US. - Home can be any location. - Military personnel. - A child who was born or died in 2009 counts as having lived for all of 2009. 	<ul style="list-style-type: none"> - Child cannot file a joint return unless only to get a refund and other exceptions.

Table 3- Individuals With No Qualifying Children

RELATIONSHIP TEST	AGE TEST	RESIDENCY TEST	JOINT RETURN TEST
<ul style="list-style-type: none"> - Filer cannot be the dependent of another person. - Filer cannot be a qualifying child of another person. 	<ul style="list-style-type: none"> - Filer must be at least 25 but under 65. 	<ul style="list-style-type: none"> - Filer must have lived in the U.S. for more than half a year. 	<ul style="list-style-type: none"> - None.

¹ Website: IRS.gov: EITC Income Limits, Maximum Credit Amounts and Tax Law Updates

IRS Response to Los Angeles Replication of New York City Model

NYC collects a Personal Income Tax from working individuals living in NYC. This tax structure has allowed NYC, a tax agency, to enter into an information-sharing agreement with the IRS which has enabled NYC to identify individuals who are potentially eligible to receive EITC Credits in prior years. As a result, NYC launched the EITC Mailing Project and, in 2007, 840,000 NYC residents received EITC credits totaling \$2.2 billion². The IRS indicates that the NYC model cannot be replicated in Los Angeles. The IRS cannot share taxpayer data with the City of Los Angeles given that the City does not have a Local Income Tax and therefore does not qualify as a "tax agency" for data-sharing purposes.

IRS Alternative EITC Effort

As an alternative to THE NYC EITC Mailing Project, the IRS agreed to launch a statewide EITC Initiative in California. Through the initiative, the IRS will reach out to residents who appear to be eligible for, but did not claim the EITC Credit on their 2009 federal returns. According to the IRS, approximately 46,000 notices will be mailed to eligible California residents in early November 2010. If all 46,000 potential EITC recipients were to receive the maximum allowable amount of \$5,657, this initiative could bring approximately \$260 million into the state, although reaching this amount is not likely given various qualifying factors. Table 1 above provides the income limits and Tables 2 and 3 show the factors such as marital status, income limits, family size and others that are used to determine the actual amount of the EITC per individual filer. Table 4 below provides a sample of possible reimbursement amounts by income level, number of qualifying children and marital status. The rows in bold indicate the maximum amount for which an individual could receive a reimbursement. For example, a single individual, with no children could receive \$2 if their earned income is at most \$13,440.

Table 4- Sample EITC Reimbursement

		SINGLE, HEAD OF HOUSEHOLD, WIDOWER				MARRIED FILING JOINTLY			
If Adjusted Gross Income and Earned Income are (\$)		No Children	One Child	Two Children	Three Children	No Children	One Child	Two Children	Three Children
At least	But less	\$	\$	\$	\$	\$	\$	\$	\$
1	50	2	9	10	11	2	9	10	11
1,000	1,050	78	349	410	461	78	349	410	461
2,000	2,050	155	689	810	911	155	689	810	911
3,000	3,050	231	1,029	1,210	1,361	231	1,029	1,210	1,361
4,000	4,050	308	1,369	1,610	1,811	308	1,369	1,610	1,811
5,000	5,050	384	1,709	2,010	2,261	384	1,709	2,010	2,261
6,000	6,050	457	2,049	2,410	2,711	457	2,049	2,410	2,711
7,000	7,050	457	2,389	2,810	3,161	457	2,389	2,810	3,161
8,000	8,050	414	2,729	3,210	3,611	457	2,729	3,210	3,611
9,000	9,050	338	3,043	3,610	4,061	457	3,043	3,610	4,061
10,000	1,050	261	3,043	3,610	4,061	457	3,043	3,610	4,061
13,400	13,450	2	3,043	5,028	5,657	380	3,043	5,028	5,657
15,000	15,050	0	3,043	5,028	5,657	261	3,043	5,028	5,657
18,400	18,450	0	2,723	4,606	5,234	2	3,043	5,028	5,657
20,000	20,050	0	2,467	4,269	4,897	0	3,043	5,028	5,657
25,000	25,050	0	1,668	3,216	3,844	0	2,467	4,269	4,897
30,000	30,050	0	869	2,163	2,791	0	1,668	3,216	3,844
35,000	35,050	0	70	1,110	1,738	0	869	2,163	2,791
35,450	35,500	0	1	1,015	1,644	0	797	2,068	2,697
40,000	40,050	0	0	57	685	0	70	1,110	1,738
40,250	40,300	0	0	5	633	0	30	1,057	1,686
40,450	40,500	0	0	0	591	0	1	1,015	1,644
43,250	43,300	0	0	0	3	0	0	425	1,054
45,000	45,050	0	0	0	0	0	0	57	685
45,250	45,300	0	0	0	0	0	0	5	633
48,250	48,279	0	0	0	0	0	0	0	3

² Assistant Commissioner Sam Miller from the New York City Department of Finance. November 17, 2009.

Los Angeles EITC Initiative

According to the IRS, there are approximately 12,649 individuals or families who may qualify for the EITC Credit in Los Angeles County. If all 12,649 potential EITC recipients were to receive the maximum allowable amount of \$5,657, this initiative could bring approximately \$71 million into the County.

Based on data provided by the IRS, preliminary calculations show that there are approximately 7,332 tax payers in the City who may be eligible for an EITC refund for Tax Year 2009. The IRS provided the City with a list of zip codes and the number of potential EITC recipients by zip code. With the assistance of the City Planning Department (DCP), each zip code was matched to a corresponding Council District. However, in many cases, zip codes were included in more than one Council District. To the extent possible, we eliminated duplicative data to arrive at the total number of potential EITC recipients in the City. Table 5 shows the number of eligible EITC recipients in California, Los Angeles County, City of Los Angeles and by Council District, based on information from the IRS. The table also provides the range of dollars that would be funneled into each district according to the number of potential 2009 EITC recipients and the minimum and maximum credit allowed for Tax Year 2009. The following are the maximum EITC credit levels allowed for Tax Year 2009:

- \$5,657 for individuals filing with three or more qualifying children.
- \$5,028 for individuals filing with two qualifying children.
- \$3,043 for individuals filing with one qualifying child.
- \$457 for individuals filing with no qualifying children.

The American Recovery and Reinvestment Act (ARRA) provides a temporary increase in EITC and expands the credit for workers with three or more qualifying children. These changes are temporary and apply only to Tax Years 2009 and 2010. Given that the City's constituents and families throughout the country continue to suffer the effects of a challenging economy, we recommend that the Council adopt a Resolution urging the United States Congress to extend the EITC Credit to workers with three or more children until 2014, for an additional three-year period.

Note: The EITC Credits in Table 5 represent the reimbursement amounts for Single individuals earning between \$5,950 and \$7,500 with no children. The Maximum EITC Credit is for Single individuals earning between \$12,550 and \$16,450, with three or more qualifying children, or married individuals filing jointly with three or more qualifying children. Calculations based on data provided by IRS and DCP. Reaching the maximum in every individual case is not likely.

Table 5- Estimated Reimbursement by Council District

Government Entity	No. of Recipients	Lower Range EITC Credit	Maximum EITC Credit	Estimated Range of Dollars by Region	
California	46,000 +	\$457	\$5,657	\$2,102,2000	\$260,222,000
Los Angeles County	12,646	\$457	\$5,657	\$5,779,222	\$71538422
City of Los Angeles	7,332	\$457	\$5,657	\$3,350,724	\$41,477,124
Council District					
1	320	\$457	\$5,657	\$146,240	\$1,810,240
2	567	\$457	\$5,657	\$259,119	\$3,207,519
3	361	\$457	\$5,657	\$164,977	\$2,042,177
4	586	\$457	\$5,657	\$267,802	\$3,315,002
5	610	\$457	\$5,657	\$278,770	\$3,450,770
6	317	\$457	\$5,657	\$144,869	\$1,793,269
7	258	\$457	\$5,657	\$117,906	\$1,459,506
8	361	\$457	\$5,657	\$164,977	\$2,042,177
9	417	\$457	\$5,657	\$190,569	\$2,358,969
10	352	\$457	\$5,657	\$160,864	\$1,991,264
11	816	\$457	\$5,657	\$372,912	\$4,616,112
12	403	\$457	\$5,657	\$184,171	\$2,279,771
13	388	\$457	\$5,657	\$177,316	\$2,194,916
14	640	\$457	\$5,657	\$292,480	\$3,620,480
15	936	\$457	\$5,657	\$427,752	\$5,294,952

EITC Impact on Welfare Benefits

According to the IRS, any refund that an individual receives due to the EITC Credit and any advance EITC payments are not considered income when determining whether the individual is eligible for any of the following programs:

- Medicaid and Supplemental Security Income (SSI)
- Supplemental Nutrition Assistance Program (SNAP, formerly Food Stamps)
- Low-Income Housing.
- Temporary Assistance to Needy Families³

San Francisco Working Families Credit (WFC)⁴

The WFC is a locally funded and administered tax credit for employed low-income tax filers with children who qualify for the federal EITC and live in the City of San Francisco. A 2006 report by the Brookings Institution states that WFC was inspired by the need to increase the number of local applicants for the federal EITC, promote saving and asset building for working families, and help retain families in San Francisco. San Francisco's WFC Program is funded by general city revenue and private contributions. For the initial year, 2005, Mayor Gavin Newsom pledged half the estimated \$6 million cost from San Francisco's General Fund and sought private sector contributions for the remainder of the funds. An agreement was reached through a formal MOU with H&R Block who provided partial funding for the project. With the assistance of the IRS to confirm eligibility, the City of San Francisco was able to implement a two-year pilot program in 2005. The Brookings Institution reports that over 11,000 working San Francisco Families applied for the WFC Program in its first year and over 9,600 checks were issued with an average benefit of \$220 for a total of \$2,112,000. We have included a recommendation directing City staff to explore the feasibility of developing a local EITC strategy similar to San Francisco that would fit the tax structure of the City of Los Angeles and would be consist with the City's current financial situation.

³ According the City of Los Angeles Community Development Department TANF is not considered earned income, and therefore would not be counted against an EITC Credit.

⁴ May 2006 The Brookings Institution, Survey Series

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MOTION

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The federal Earned Income Tax Credit (EITC), first enacted in 1975, is a tax credit for working adults who make low wages. The EITC is widely considered one of the most effective anti-poverty policies in the United States.

A number of studies show that the Earned Income Tax Credit has been successful in both lifting families out of poverty and in moving individuals and families from cash assistance welfare to the workforce, since the credit provides extra incentive to work by allowing more earned income to be kept.

Depending on one's filing status, the tax credit can be significant—up to \$4,400 in tax relief for working families with more than one qualifying dependent. Yet the Internal Revenue Service estimates that each year 20 to 25% of those eligible for the Earned Income Tax Credit fail to claim the credit and therefore lose out on hundreds or thousands of dollars per household.

On a city-wide level, this translates into millions of unclaimed dollars that could have helped our most deserving families. In the City of Los Angeles, for example, one study conservatively estimates that 15% of workers qualified but failed to file for the EITC in tax year 2005-- translating into more than forty thousand households that missed out on over \$80 million in federal tax relief dollars.

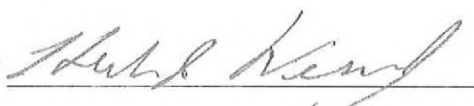
I THEREFORE MOVE, that the Jobs and Business Development Committee review and propose to Council options for improving receipt of the Earned Income Tax Credit (EITC), to bring more dollars to the pockets of working Los Angeles households in this time of great economic need.

PRESENTED BY



RICHARD ALARCON
Councilmember, 7th District

SECONDED BY



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