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OHIO LEGISLATIVE SERVICE COMMISSION

Office of Research and Drafting

Legislative Budget Office

H.B. 114
(l_133_0363-1)
133rd General Assembly

Fiscal Note & Local Impact Statement

Click here for H.B. 114's Bill Analysis

Version: In House Ways and Means

Primary Sponsors: Reps. Skindell and Crawley

Local Impact Statement Procedure Required: Yes

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Highlights

Fund	FY 2021	FY 2022	Future Years
State General Revenue Fund			
Revenues	Loss of $201 million	Loss of $205 million	Annual losses of $205 million
Local Government and Public Library funds (counties, municipalities, townships, and public libraries)			
Revenues	Loss of $7 million	Loss of $7 million	Annual losses of $7 million

Note: The state or school district fiscal year runs from July 1 through June 30 and is designated by the calendar year in which it ends. For other local governments, the fiscal year is identical to the calendar year.

- The bill makes one-third of the earned income credit (EIC) refundable beginning with the tax year the bill becomes effective. Continuing law sets the Ohio EIC equal to 30% of the taxpayer's federal earned income tax credit (EITC), and H.B. 114 enables a portion to be refundable while the remaining share will continue as a nonrefundable credit.
- Enabling Ohio taxpayers to claim a partially refundable version of the current credit in tax year 2020 would reduce statewide personal income tax (PIT) liability by an estimated $208 million. This estimate should be considered rather rough because it depends on the number of eligible taxpayers who begin claiming the newly modified Ohio credit.
- Under current law, the GRF would bear 96.62% of any revenue loss under the income tax during the current biennium, while the Local Government Fund (LGF) would bear 1.68% and the Public Library Fund (PLF) would bear 1.70% of any such revenue loss.

Detailed Analysis

Existing personal income tax (PIT) law allows for a nonrefundable earned income credit (EIC). As of tax year (TY) 2019, the state credit equals 30% of the federal earned income tax credit (EITC) claimed on the taxpayer's federal tax return. H.B. 114 changes the nonrefundable status of the Ohio EIC to partially refundable. Beginning with the tax year during which the bill becomes effective (i.e., TY 2020 if signed by the Governor on or before October 1, 2020, otherwise, TY 2021), one-third of the Ohio EIC becomes refundable and the remaining two-thirds continues as a nonrefundable credit.

In practice, the state income tax form would likely have two separate lines for the Ohio EIC: (1) the nonrefundable credit equal to 20% of the federal EITC, and (2) the refundable credit equal to 10% of the federal EITC. This fiscal note assumes TY 2020 would be the first year that taxpayers could claim refunds, which reduces state revenues beginning in FY 2021 as PIT returns are filed.

Fiscal effect

The bill creates a new incentive for taxpayers to claim the Ohio EIC on their state tax return. Under current law, the credit is wholly nonrefundable, and PIT filers with a taxable income at or below $21,750 in TY 2019 do not owe any amount.[1] For these taxpayers, and others with little or no PIT liability, there is scant benefit to claim the current nonrefundable credit, but there may be costs associated with filling out the Ohio EIC portion of their state tax return. Empirical evidence from TY 2017 shows that 931,330 Ohio-based taxpayers claimed the EITC on their federal return. However, only 768,311 (approximately 82% of the federal total) personal income tax filers claimed the EIC on their state tax form.

The underrepresentation of EIC claims among PIT filers necessitates an assumption about taxpayers' behavioral response to the partially refundable policy in H.B. 114. When estimating the fiscal effect for the bill, LBO assumed 95% of all eligible taxpayers would claim this refundable credit on their TY 2020 PIT return, an increase from the current 82% utilization rate. The estimated revenue loss should be considered rough because, while the percentage would almost certainly increase, LBO economists are not aware of a reliable basis for projecting the increase in this utilization rate. That said, if the actual percentage turned out to be 90%, the revenue loss would be about $10 million lower; conversely, it would be about $10 million higher if 100% of eligible taxpayers utilized the refundable credit.

The table below displays estimates of the average PIT refund in a given income category, and then multiplies that amount by the projected number of tax returns. The resulting PIT revenue loss for each income category is found in the right hand column of the table. Since these income classifications are predicated on federal taxpayer information, they reflect federal adjusted gross income (FAGI) rather than Ohio taxable income.

[1] R.C. 5747.02 requires the Tax Commissioner to revise income tax brackets for inflation every August, so the threshold will increase for TY 2020.

Estimated Impact of Refundable Ohio EIC in TY 2020, as Compared to Baseline Law			
Income Category	**Average PIT Refund per Tax Return**	**Number of Tax Returns**	**PIT Revenue Loss (in millions)**
$1 to $10,000	$112	172,683	$19.3
$10,001 to $25,000	$351	360,319	$126.5
$25,001 to $50,000	$209	296,479	$62.0
$50,001 to $75,000	$6	17,850	$0.1
Above $75,000	$0	0	$0
Total	**N/A**	**847,331**	**$207.9**

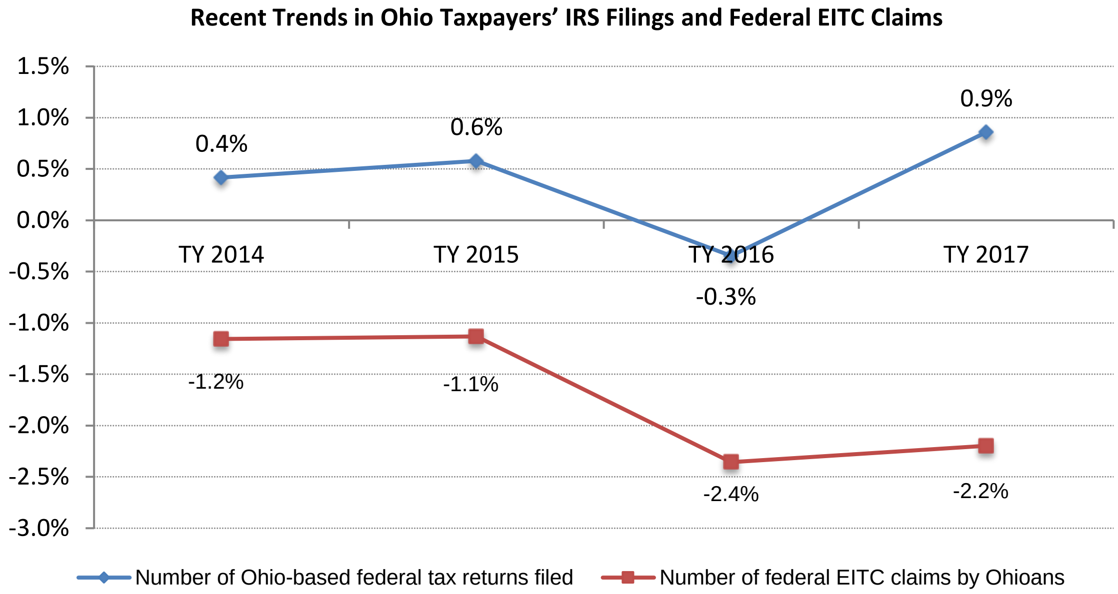
Note: Totals computed using unrounded numbers. Estimated using sample of PIT returns filed for TY 2017.

The table only estimates PIT losses for TY 2020, which corresponds with FY 2021 receipts, but foregone revenue amounts in future years would be comparable absent any forthcoming tax policy changes at the state or federal level. The GRF would bear 96.62% of any revenue loss from the income tax during the current biennium under an uncodified provision of H.B. 166 of the 133rd General Assembly, while the Local Government Fund (LGF) would bear 1.68% and the Public Library Fund (PLF) would bear 1.70% of any such revenue loss.[2]

Trends in federal EITC claims

As noted above, in TY 2017, the most recent year for which the Internal Revenue Service (IRS) has published the data, 931,330 tax returns filed by Ohio residents claimed the federal EITC, in amounts totaling $2.26 billion. The overall number of federal EITC claims has declined in recent years. The chart below illustrates the trends among Ohio taxpayers over the most recent five-year period, TY 2013 to TY 2017. IRS statistics for Ohio-based taxpayers generally show the number of tax returns increasing every year, as evidenced by the blue line and its (mostly) positive annual percentage changes. Meanwhile, the number of taxpayers claiming the EITC on their federal return (refer to the red line) has steadily declined over this same duration.

[2] Under current law, the GRF share would revert to 96.68% of the revenue loss beginning July 1, 2021, and the LGF and PLF shares would each revert to 1.66%; these shares are specified in codified law.



Nevertheless, the longer history of this federal tax credit demonstrates it is counter cyclical; the number of EITC claims declines during economic expansion but increases immediately after recessions. Although not illustrated by the above chart, claims rose from TY 2003 through TY 2011, albeit not completely under organic circumstances. Some of the growth in EITC claims beginning in TY 2009 was also attributable to an expanded federal eligibility policy authorized by the American Recovery and Reinvestment Act of 2009 (or "federal stimulus" bill). The PIT estimate generated for this fiscal note by LBO assumed continued economic expansion, but state revenue losses could exceed these enumerated amounts during another recession. Finally, the fiscal note assumes no new state or federal policy changes will materialize, other than annual inflation adjustments for the EITC.

Synopsis of Fiscal Effect Changes

The substitute bill reduces the refundable value of the Ohio EIC from 30% to 10% of the taxpayer's EITC, as claimed on their federal tax return. By doing so, the substitute bill reduces annual PIT revenue losses attributable to the As Introduced version by approximately $381 million. Separately, the substitute bill replaces the TY 2019 effective date with a later date in either TY 2020 or TY 2021. Delaying the effective date of the substitute bill prevents the GRF from incurring a revenue loss up to $201 million during FY 2020 (and also possibly in FY 2021, depending on the timing of enactment).

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