

Fact Sheet: Tax Bill Offers Earned Income Tax Credit Upside, Flat Tax Downside

Analysis of Substitute Version of House Bill 329 (LC 43 0601S), February 27, 2017

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Georgia lawmakers are considering a large income tax proposal that contains a mix of positive reforms and measures that raise significant concerns. Some aspects of the bill including a new Georgia [Earned Income Tax Credit](#) (EITC) and modest increases to personal exemptions and deductions stand to benefit many working families. In contrast, a proposed move to set a new a flat tax rate 5.4 percent provides an outsized gain to taxpayers at the very top and raises taxes for low-wage workers without children. Though not as costly as some other recent tax makeover proposals, HB 329 could also cause some headaches for Georgia lawmakers in future years as lost revenue accumulates. Lawmakers can consider targeted fixes to the bill to avoid doing more harm than good.

Revised Tax Package Proposes Four Big Changes

The substitute version of House Bill 329 includes four key income tax alterations. The first three reforms are explained in more detail in our [full five-page analysis of HB 329](#). Some details on the fourth item, new since the original proposal was filed, are included below.

- A **flat tax** of 5.4 percent to replace Georgia's graduated structure with rates from 1 percent to 6 percent
- A new nonrefundable **Earned Income Tax Credit** set at a 10 percent match of the federal credit
- An overdue **fix to the double deduction loophole** that allows some taxpayers to deduct the value of their state income taxes twice
- A proposal to **index broadly available deductions to inflation**. The revised version of HB 329 proposes to gradually increase Georgia's standard deduction, personal exemption and dependent exemption by indexing them to inflation. This would slowly increase the size of Georgia's tax shield, or the amount of income families can make before owing the state's personal income tax. This sensible reform provides a modest benefit to working families over the long haul, though the change will also gradually swell the long-term cost in lost revenue. Our [comprehensive blueprint for tax reform](#) released in 2015 proposed increasing the tax shield.

The annual cost of HB 329 could range from about \$20 million to \$154 million in lost revenue, according to two separate estimates from reliable sources. The state's official fiscal note estimates the price of HB 329 at about \$19.5 million a year once fully phased-in starting in the 2019 budget year. An alternative estimate from the nonpartisan Institute on Taxation and Economic Policy in Washington, D.C. estimates the annual cost at \$154 million a year. While the potential price is not as large as some recent tax system makeover proposals, revenue losses at the top of this cost range could add an extra challenge when Georgia lawmakers need to fund vital services in the future.

Proposed Tax Reforms Create Winners and Losers

HB 329 would provide an inconsistent benefit to low- and moderate-income taxpayers depending on their circumstances. Low-wage families *with* children stand to gain under the restructuring, whereas low-wage workers *without* children stand to lose. This nuanced effect occurs because of the interplay between moving to a flat tax on one hand and enacting a new EITC on the other. Switching from Georgia's current graduated income tax to a flat rate structure raises taxes for low-income people across the board. However, families with dependent children stand to gain enough from an EITC to offset that initial hike. The table below provides examples.

New Flat Tax and Earned Income Tax Credit Combine to Raise Taxes for Poor Childless Workers, Cut Them for Poor Families				
Family Type	Poverty Line	State Income Taxes Owed		Tax Change
		Under Current Law	Under HB 329	
Single, no children	\$12,060	\$226	\$352	\$ 126
Married, no children	\$16,240	\$134	\$273	\$ 140
Single, one child	\$16,240	\$242	\$98	\$ (144)
Married, one child	\$20,420	\$191	\$42	\$ (149)
Single, two children	\$20,420	\$311	\$0	\$ (311)
Married, two children	\$24,600	\$250	\$0	\$ (250)
Source: GBPI calculations based on Georgia Code Section 48 and House Bill 329 and IRS tables for Earned Income Credit				

In contrast to the nuanced effect on working families, HB 329 offers a clear benefit to affluent Georgians. An estimated 74 percent of the overall reduction in state taxes would flow to Georgians who make more than \$97,000 a year, the most affluent fifth of taxpayers. This effect is predictable because cutting the income tax *rate* provides a disproportionate tax cut to families with the most taxable income.

Targeted Fixes Can Ensure Tax Package Does More Good Than Harm

Creating a new state EITC and indexing broadly available exemptions to inflation are good things for Georgia families. Closing the double-deduction loophole is good for Georgia's finances. On the other hand, replacing Georgia's current graduated rate structure with a flat tax stands to raise taxes on low-wage workers without children and could cause some headaches for Georgia budget writers down the road. Lawmakers can consider two key changes to the HB 329 tax package to address the shortcomings.

Reconsider the shift to a flat rate structure to eliminate the likely tax increases for childless, working class Georgians. Georgia's current graduated tax structure provides a modicum of fairness to offset sales taxes, fees and other levies that fall more sharply on working families. If Georgia's top income tax rate is destined for a change, lawmakers can restructure it without upending the underlying structure of the system.

Scale back the scope of the proposed rate cut to minimize the potential long-term cost in state revenue. The personal income tax is the workhorse of Georgia's revenue system. Cutting as deep as 5.4 percent could jeopardize Georgia's ability to fully fund schools, health care and other building blocks of a strong economy.