EXHIBIT 4
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HB 360

Policy Brief
01/19/2009

Investing in Montana's Working Families: A Montana Earned Income Tax Credit (EITC)

For too many Montana workers, their low wages are not enough to adequately provide for their families. A state EITC would help Montana working families struggling to make ends meet. Economic trends have made it harder for working families to live above the poverty line. In fact, Montana currently has over 16,000 families that are working but still live in poverty. The current economic crisis will only increase the struggles for these low-income families. Unfortunately, Montana's income tax system drives many poor working families deeper into poverty. A state EITC would help ameliorate this effect on low-income taxpayers. In addition, a state EITC is one of the most efficient and effective mechanisms for stimulating our economy during the current economic downturn.

> *"States that enact EITCs can reduce child poverty, cut taxes, and increase the incentive to work for families struggling to make ends meet."*
> Center for Budget and Policy Priorities ("State Earned Income Tax Credits," October 2008).

Why Does Montana Need a State Earned Income Tax Credit?

- *Montana's Income Tax System Pushes Working Families Further into Poverty*

Montana is one of the few states in the country to impose income taxes on working families living in poverty. **We begin taxing a single worker with 2 children at a lower annual income than any other state in the country.**[1] Montana taxes a single parent household with 2 children starting at $9,600 in annual income, which is 58% of the poverty level for a family of that size. Montana taxes a two parent, 2 children family starting at $11,600 in annual income, which is 54% of the poverty level for a family of that size. By enacting a state EITC, Montana would help cushion the effect of our income tax system on families who have limited income despite their work.[2]

Key Points

- EITCs supplement the incomes of working families struggling to make ends meet despite their work.
- Montana's income tax system is one of the worst in the county in terms of the burden it places on poor and low-income working families.
- Over 16,000 families in Montana live in poverty despite the fact that they work.
- Credits targeted at low-income households are an efficient way to boost the economy through increased demand for goods and services.
- The federal EITC has enjoyed bipartisan support since its inception.
- In 2005, over 72,000 low-income working households in Montana received over $123 million through the federal EITC. The maximum federal benefit in 2008 is $4824.
- The federal EITC is the nation's most effective anti-poverty program, lifting over 4 million people - 2 million of them children - out of poverty each year.
- A state EITC set at 20% of the federal EITC would result in a maximum benefit of $943 for low-income working families, with a total cost to the state of approximately $24 million per year.

[1] Center on Budget and Policy Priorities, "The Impact of State Income Taxes on Low-Income Families," October 2008.
[2] Of course, in addition low-income workers also contribute to our tax system through pay payroll, excise and property taxes.

- *Economic Trends are Making It Even Harder for Montana Families to Make Ends Meet*

A full-time working parent earning minimum wage in 2008 made approximately $13,300, or $4,300 *under* the federal poverty line. **Over 16,000 Montana families are working but still live in poverty (almost 7% of Montana households).**[3] Unfortunately, Montana's income tax makes it even harder for many of these families to purchase basic necessities. A state EITC would help these families secure housing, groceries, childcare, transportation, and medical care during these economically challenging times.

- *Tax Credits for Low-Income Families Offer Effective Stimulus during Recessions*

Putting more money in the hands of low-income families is particularly good policy during an economic downturn. One of the basic tenets of economic policy is that increased demand for goods and services is necessary to bring an economy out of recession. **Credits targeted at low-income households are an efficient way to achieve increased demand for goods and services because low-income families are likely to spend the entire credit, resulting in an immediate boost to the economy.**

Economic stimulus proposals are often focused on job creation, but may actually create fewer jobs than proposals that focus on low and moderate-income families.[4]

> *"Lower-income households are . . . more likely to be among those with the highest propensity to spend. Therefore, policies aimed at lower-income households tend to have greater stimulative effects."*
> Congressional Budget Office ("Options for Responding to Short-Term Economic Weakness," January, 2008).

> *"Some of the proposals that policymakers apparently think of as job creators would actually preserve or create many fewer jobs than other proposals directed at families with low or moderate incomes or unemployed workers.*
> - *The main reason why the economy is shrinking and unemployment is rising is a sharp drop in demand for goods and services.*
> - *The quickest, most efficient way to bolster demand is to put money in the hands of people who will spend it quickly — namely, people who need it to cover basic expenses such as housing, food, and transportation.*
> - *Helping struggling families thus isn't an alternative to preserving and creating jobs; it's one of the most effective ways to preserve and create jobs..."*
>
> --Chad Stone, Chief Economist, Center on Budget and Policy Priorities, Jan. 9, 2009

[3] U.S. Census Bureau.

[4] Stone, Chad. "Assistance for Hard-pressed Families is one of the Best Ways to Preserve and Create Jobs: Measures Supported by Some Policymakers Would be Far Less Effective," Center on Budget and Policy Priorities, January 2009. http://www.cbpp.org/1-9-09bud.htm

What is the Federal EITC?

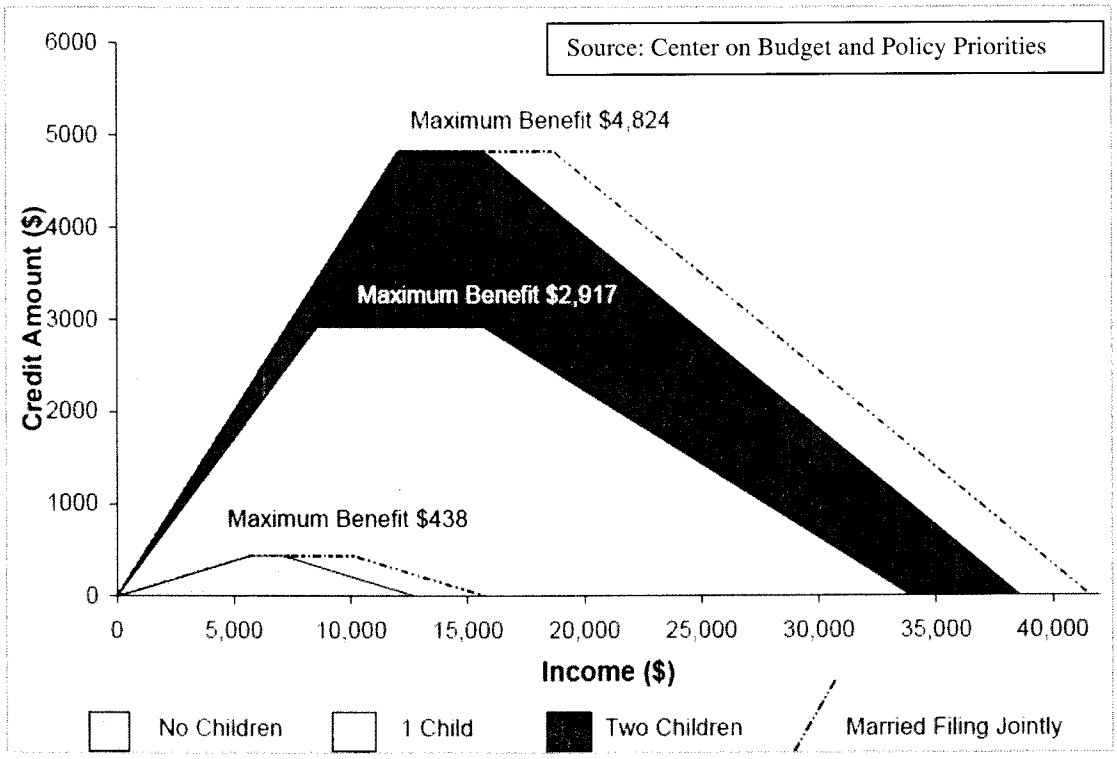
The federal EITC was created in 1975 and has long enjoyed bipartisan support. The federal EITC supplements income for low-income working families. Only people who work are eligible for the EITC. The maximum federal benefit is $4824 for 2008. The EITC is administered as a refundable tax credit meaning that recipients receive a refund when their credit amount is greater than their total tax liability. Presidents Reagan, George H.W. Bush and Clinton all proposed expansions of the federal EITC. In 2005, over 72,000 low-income working households in Montana received over $123 million through the federal earned income tax credit.[5]

> *"[The EITC is] the best anti-poverty, the best pro-family, the best job creation measure to come out of Congress."*
> -Former President Ronald Reagan

How Does the Federal Earned Income Tax Credit Work?

Eligibility for the federal EITC is limited to low income families with earnings from work. The amount of credit available depends on family size[6] and income. The credit varies with income in three ranges: (1) the phase-in range where EITC benefits increase with earnings; (2) a plateau where the maximum EITC amount remains constant; and (3) the phase-out range where benefits decline as earnings increase (Figure 1). Most families claim their EITC when they file their federal income tax returns. A small number of families choose to receive the credit throughout the year as a supplement to their paycheck through the advance payment option.

Figure 1- Value of Federal Earned Income Tax Credit, 2008



[5] Brookings Institute, EITC Interactive Website, http://www.brookings.edu/projects/EITC.aspx.
[6] Eligibility and maximum benefits are significantly reduces for individuals without children (See Figure 1).

Has the Federal EITC Worked?

Yes.

- **The federal EITC lifts more than 4 million people, including 2 million children, out of poverty each year.**[7]
- Federal and state EITCs have been found to increase workplace participation among eligible families.[8]
- Research shows that families use the EITC to pay for basic needs, home repair, commuting expenses, education and training, and other expenditures to improve employability.[9]
- Recognizing the effectiveness of the federal EITC, twenty-four states (a majority of states with income tax systems) have enacted state EITCs to further supplement the income of working families.[10]

How Would a State EITC Work?

Most state EITCs are patterned after the federal credit (see Table 1 for details about other states' EITCs). A state EITC would give workers a refundable tax credit equal to a percentage of the federal EITC. By linking state eligibility rules to those of the federal credit, Montana can take advantage of federal compliance efforts and coordinated efforts to publicize the availability of the credits. Like the federal EITC, a state EITC would be refundable, meaning that it would first be used to reduce a family's tax liability, with any remainder returned to the family in the form of a refund. **A state EITC set at 15% of the federal EITC would result in a maximum benefit of $724 for low-income working families, with a total cost to the state of approximately $18 million per year.**

[7] Center on Budget and Policy Priorities. "Earned Income Tax Credit," January 2008.

[8] Nada Eissa and J.B. Liebman. "Labor Supply Response to the Earned Income Tax Credit." *Quarterly Journal of Economics*, Vol. 111 No. 2 (May 1996) pp. 605-637: For a review of the research around the impact of the EITC on workforce participation, see Timothy Holt, "The Earned Income Tax Credit at 30: What We Know," The Brookings Institution, February 2006

[9] Timothy M. Smeeding, K.R. Phillips and M. O'Connor. "The EITC: Expectation, Knowledge, Use and Economic and Social Mobility." *The National Tax Journal*, Vol. 53, No. 4, Part 12 (December 2000) pp1187-1210.

[10] Jason A. Levitis and Andrew C. Nicholas. "The Impact of State Income Taxes on Low-Income Families in 2007," Center for Budget and Policy Priorities, October 2008

Table 1

State Earned Income Tax Credits Based on the Federal EITC

State	Percentage of Federal Credit (Tax Year 2006 Except as Noted)	Refundable	Workers Without Qualifying Children Eligible?
Delaware	20%	No	Yes
District of Columbia	40%	Yes	Yes
Indiana	6% (to 9% in 2009)	Yes	Yes
Illinois	5%	Yes	Yes
Iowa	7%	Yes	Yes
Kansas	17%	Yes	Yes
Louisiana	3.5%	Yes	Yes
Maine	5%	No	Yes
Maryland[a]	25%	Yes	Yes
Massachusetts	15%	Yes	Yes
Michigan	10% (to 20% in 2009)	Yes	Yes
Minnesota[b]	Average 33%	Yes	Yes
Nebraska	10%	Yes	Yes
New Jersey	22.5% (to 25% in 2009)	Yes	Yes
New York[c]	30%	Yes	Yes
North Carolina[d]	3.5% (to 5% in 2009)	Yes	Yes
Oklahoma	5%	Yes	Yes
Oregon[e]	6%	Yes	Yes
Rhode Island	25%	Partially[f]	Yes
Vermont	32%	Yes	Yes
Virginia	20%	No	Yes
Washington	5% (to 10% in 2010)[g]	Yes	Yes
Wisconsin	4% — one child 14% — two children 43% — three children	Yes	No

Notes: From 1999 to 2001, Colorado offered a 10% refundable EITC financed from required rebates under the state's "TABOR" amendment. Those rebates, and hence the EITC, were suspended beginning in 2002 due to lack of funds and again in 2005 as a result of a voter-approved five-year suspension of TABOR. Under current law, the EITC is projected to resume in 2011, but a recent income tax cut that also depends on the rebates is likely to exhaust the funds, leaving the EITC unfunded.

[a] Maryland also offers a non-refundable EITC set at 50 percent of the federal credit. Taxpayers in effect may claim either the refundable credit or the non-refundable credit, but not both.
[b] Minnesota's credit for families with children, unlike the other credits shown in this table, is not expressly structured as a percentage of the federal credit. Depending on income level, the credit for families with children may range from 25 percent to 45 percent of the federal credit; taxpayers without children may receive a 25 percent credit.
[c] Should the federal government reduce New York's share of the TANF block grant, the New York Credit would be reduced automatically to the 1999 level of 20 percent.
[d] North Carolina's EITC is scheduled to expire in 2013.
[e] Oregon's EITC is scheduled to expire at the end of 2013.
[f] Rhode Island made a very small portion of its EITC refundable effective in TY 2003. In 2006, the refundable portion was increased from 10 percent to 15 percent of the nonrefundable credit (i.e. 3.75 percent of the federal EITC)
[g] Washington's EITC is worth five percent of the federal EITC or $25, whichever is greater. When the matching rate rises to ten percent in 2010, the minimum value will rise to $50.

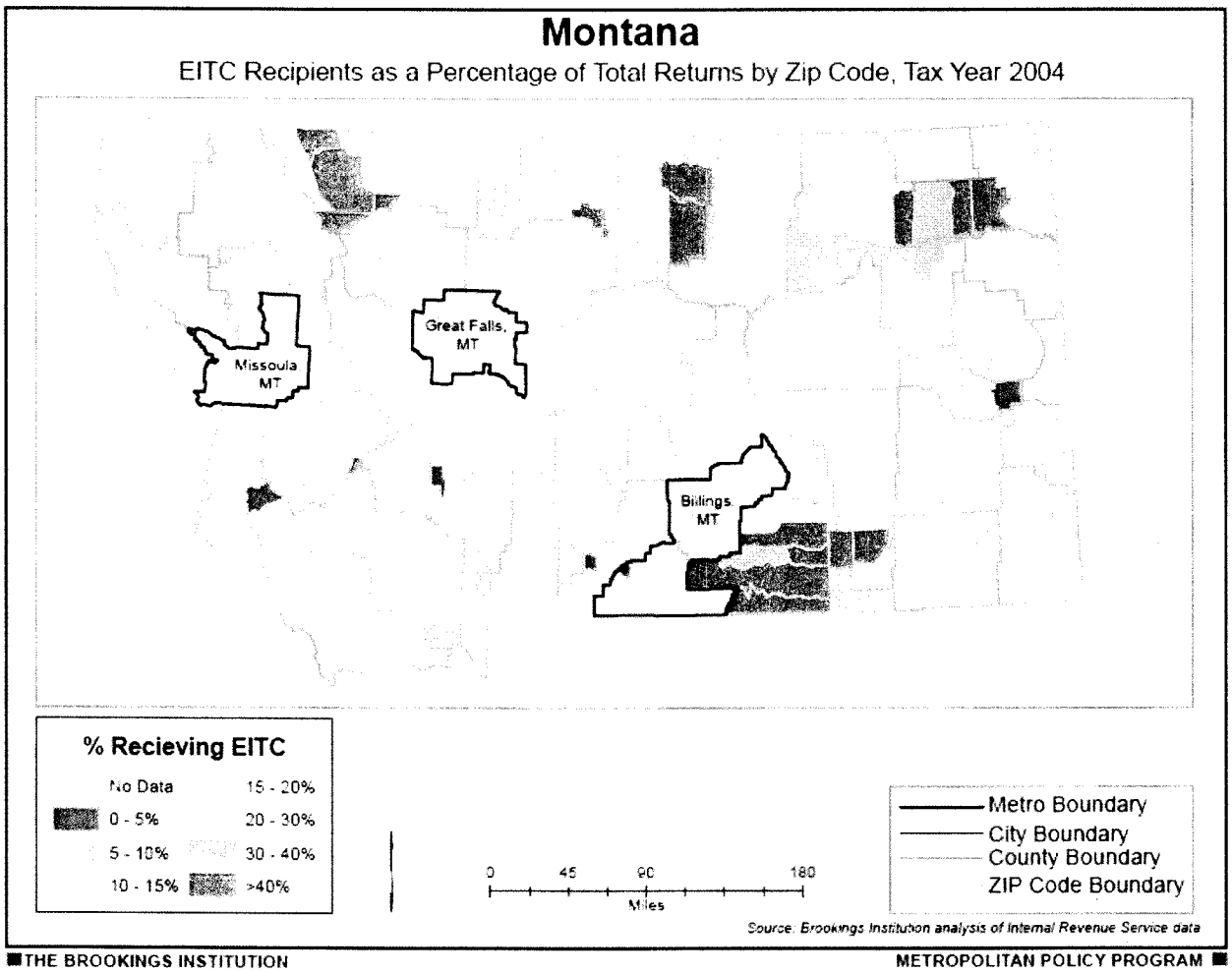
Source: Center on Budget and Policy Priorities

Who Would Benefit from a Montana EITC?

- *Individuals and Families.*

Figure 2 maps the recipients of the federal EITC. Appendices B and C show detailed information about the federal EITC by Senate and House districts. Over 72,000 Montana households (16.6%) received the federal EITC in 2005 and would therefore benefit from a state EITC.

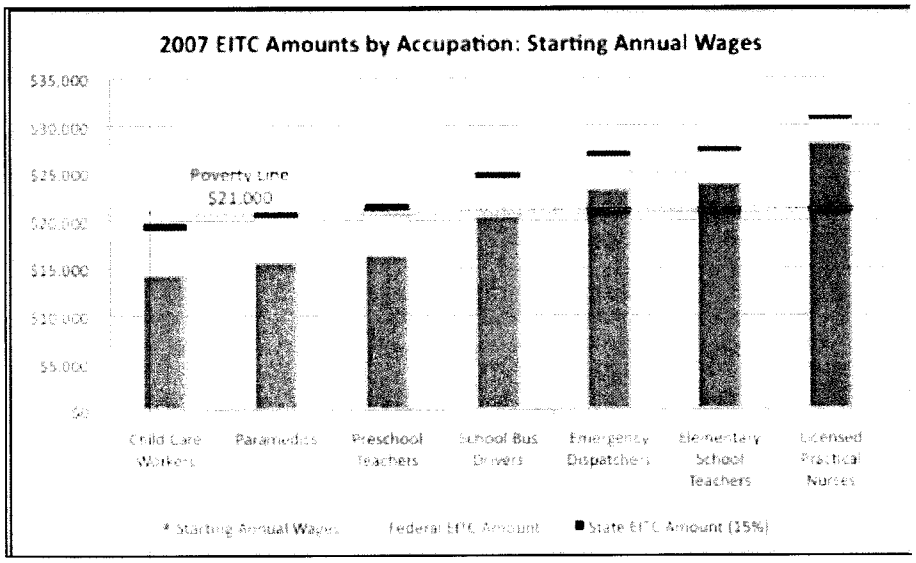
Figure 2: Federal EITC Recipients by Zip Code in Montana



Child care workers, paramedics, preschool teachers, school bus drivers, emergency dispatchers, elementary school teachers, licensed practical nurses, and workers in numerous other occupations would be eligible for the EITC based on average starting salaries (see figure 3).

The income of a family of four supported by a full-time worker earning $7.50/hour still falls well below the poverty level. The same family would be raised out of poverty by the combination of a state and federal EITC). The increase in income from the federal and state EITC is equivalent to a wage increase of $2.67/hour.

Figure 3



Assumptions: *Married couple, filing jointly*
Two or more children
State EITC assessed at 15 % of federal

Source: IRS, the Center for Policy and Budget Priorities, and the Montana Dept. of Labor and Industries.

- *Employers*

The EITC serves as a wage supplement, helping business find labor at affordable rates while workers earn enough to make ends meet. In short, the EITC is a wage supplement that makes work pay. The federal EITC combined with a state EITC is equivalent to a $2.67/hour raise for a minimum wage worker. Fifty-four percent of EITC recipients work for private business (see Appendix A for this and more information about individuals and families eligible for the EITC).

- *Rural areas and small towns*

While nationally, most beneficiaries are in large cities, rural areas and small towns get a disproportionate amount of the benefits per capita. In the Montana, 65% (47,683) of EITC recipients in 2005 resided in rural areas bringing over $82 million to their communities.[11]

- *The Economy.*

The Federal EITC is expected to bring $135 million into the Montana economy in 2009. A state EITC at 20% of the federal would pump more than $18 million into Montana's communities.[12] By placing the money in the hands of the people most likely to spend it, a state EITC would increase demand for goods and services and boost the economy.

[11] Kneebone, Elizabeth. 2008. "Bridging the Gap: Refundable Tax Credits in Metropolitan and Rural America. The Brookings Institute: Metropolitan Policy Program.

[12] Dillon, Thale. "Summary of Economic Estimates of the State and Federal Earned Income Tax Credits for Montana." Bureau of Economic and Business Research, University of Montana (2008).

Conclusion

Too many hard-working parents in Montana are living in poverty and struggling to meet their families' needs. By enacting a state EITC, Montana could help make work pay for these families, cushion the effect of our income tax system on families living in poverty, and spur growth in our economy. Montana should join the majority of other states with income tax systems who have recognized these benefits and enacted state-level EITCs.

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Appendix A

CHARACTERISTICS OF EITC-ELIGIBLE TAXPAYERS, 2007

STATE:

Montana

The Metropolitan Policy Program at Brookings

EITC-ELIGIBLE POPULATION

Total EITC-Eligible Tax Units 86,493

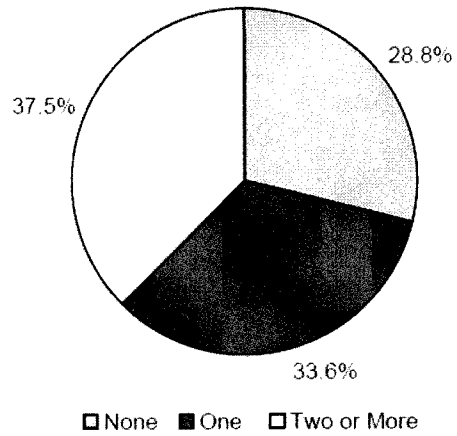
Total Population in EITC-Eligible Units 233,444

EITC-ELIGIBLE FILING UNIT CHARACTERISTICS

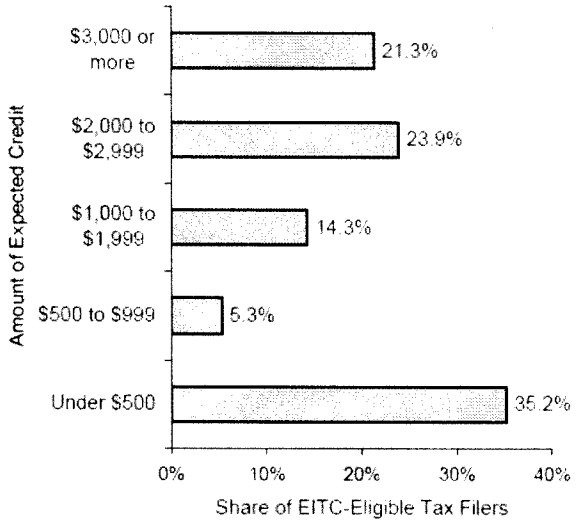
Filing Status

Married, Filing Jointly	25.6%
Head of Household	49.4%
Single	25.0%

Number of Qualifying Children



Size of Expected Earned Income Tax Credit

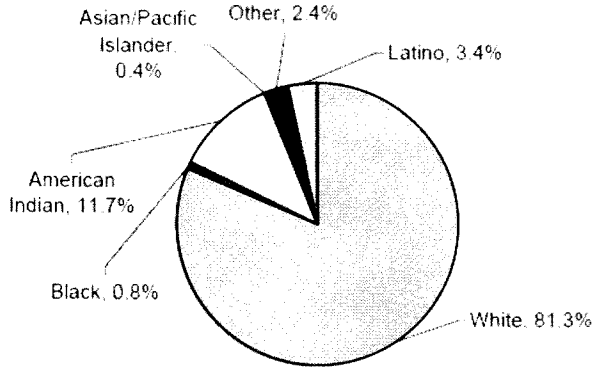


Adjusted Gross Income

$1 to $4,999	18.7%
$5,000 to $9,999	19.5%
$10,000 to $14,999	19.4%
$15,000 to $19,999	12.6%
$20,000 to $24,999	11.1%
$25,000 to $29,999	7.3%
$30,000 to $39,999	11.4%

EITC-ELIGIBLE TAX FILER CHARACTERISTICS

Race and Ethnicity of Taxpayer

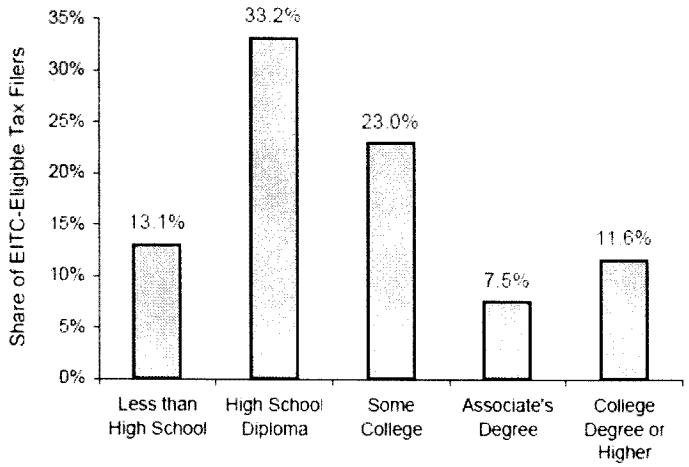


Age of Taxpayer

Under 25 years	11.7%
25 to 34 years	32.8%
35 to 44 years	22.7%
45 to 54 years	20.2%
55 years and over	12.6%

EITC-ELIGIBLE TAX FILER CHARACTERISTICS (CONTINUED)

Highest Level of Education Attained by Taxpayer



Home Ownership

Owner-occupied, with mortgage	30.8%
Owner-occupied, no mortgage	17.3%
Renter-occupied	46.9%

Receipt of Food Stamps

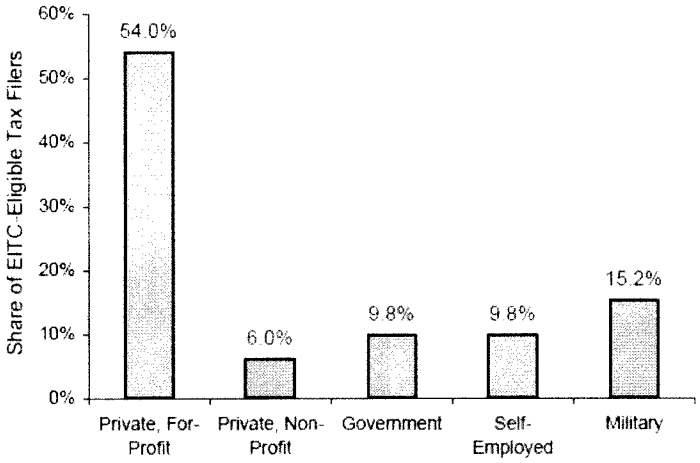
Share of tax filers in households that receive food stamps	26.0%

Language Spoken at Home

English	94.7%
Other	5.3%

* "Other" includes any language that is spoken by (a) less than 1% of taxpayers, or (b) less than 2,000 taxpayers in total.

Sector of Work for Taxpayers



* Categories may not add to 100%. Remainder represents taxpayers who identified themselves as unemployed.

Top Five Occupations

Office Administration	14.3%
Construction/Mining	11.7%
Food Preparation	9.9%
Maintenance	9.5%
Sales	9.1%

Top Five Industries

Retail Trade	13.6%
Healthcare	13.1%
Construction	12.0%
Accommodation/Food Services	12.0%
Education	5.6%

Appendix B: EITC Returns by Montana State Senate District, 2005 Tax Year

Senate District	Total returns	EITC returns	% of Returns with EITC	EITC amt ($)
District 1	7,790	1,561	20.04%	2,718,210
District 2	10,791	1,683	15.60%	2,937,427
District 3	8,771	1,421	16.20%	2,466,068
District 4	8,990	1,479	16.45%	2,569,845
District 5	12,172	1,986	16.32%	3,384,911
District 6	8,391	1,778	21.19%	3,241,744
District 7	8,731	1,631	18.68%	2,829,154
District 8	7,500	2,901	38.67%	5,782,264
District 9	8,067	1,163	14.42%	1,872,714
District 10	8,728	1,514	17.35%	2,574,497
District 11	9,331	1,816	19.46%	3,069,489
District 12	6,348	1,260	19.85%	2,188,042
District 13	8,745	1,241	14.19%	2,114,781
District 14	8,578	1,172	13.67%	2,039,754
District 15	8,321	1,309	15.73%	2,203,490
District 16	6,392	2,458	38.45%	4,973,198
District 17	7,879	1,437	18.24%	2,614,923
District 18	8,472	1,317	15.55%	2,251,061
District 19	8,675	1,147	13.23%	1,951,795
District 20	8,567	1,388	16.20%	2,325,031
District 21	6,178	2,596	42.03%	5,428,174
District 22	7,768	1,399	18.01%	2,456,768
District 23	8,400	1,199	14.28%	2,075,479
District 24	9,371	1,261	13.46%	2,315,441
District 25	9,115	1,454	15.95%	2,447,985
District 26	9,660	1,710	17.71%	2,888,534
District 27	8,790	1,454	16.54%	2,409,610
District 28	8,616	945	10.97%	1,553,828
District 29	8,997	1,007	11.19%	1,732,919
District 30	8,461	1,099	12.99%	1,814,794
District 31	9,238	1,377	14.90%	2,086,282
District 32	9,425	1,003	10.64%	1,284,583
District 33	9,379	981	10.45%	1,181,613
District 34	11,566	1,615	13.97%	2,612,855
District 35	11,581	1,394	12.04%	2,022,035
District 36	8,686	1,365	15.72%	2,314,976
District 37	7,262	1,203	16.57%	2,051,569
District 38	7,553	1,264	16.74%	2,168,728
District 39	8,420	1,136	13.49%	1,920,939
District 40	10,200	1,389	13.62%	2,207,278
District 41	8,395	1,148	13.68%	1,809,134
District 42	8,140	1,138	13.98%	1,924,066
District 43	7,096	1,244	17.54%	2,027,214
District 44	8,533	1,547	18.13%	2,754,780
District 45	8,531	1,418	16.62%	2,502,919
District 46	8,161	1,437	17.61%	2,116,691
District 47	8,011	1,163	14.52%	1,731,764
District 48	10,140	1,569	15.47%	2,302,555
District 49	9,961	1,613	16.19%	2,463,730
District 50	10,077	1,649	16.36%	2,477,484

Appendix C: EITC Returns by Montana State House District, 2005 Tax Year

House District	Total returns	EITC returns	% of Returns with EITC	EITC amt ($)
District 1	3,740	773	20.68%	1,361,103
District 2	4,050	788	19.45%	1,357,107
District 3	5,763	1,000	17.36%	1,840,479
District 4	5,008	680	13.57%	1,091,436
District 5	4,281	708	16.54%	1,269,612
District 6	4,494	714	15.88%	1,197,871
District 7	4,173	687	16.45%	1,192,775
District 8	4,827	794	16.45%	1,379,851
District 9	4,681	672	14.37%	1,133,148
District 10	7,495	1,314	17.54%	2,252,966
District 11	4,608	841	18.24%	1,509,427
District 12	3,783	937	24.77%	1,732,430
District 13	4,139	823	19.88%	1,453,732
District 14	4,591	808	17.61%	1,375,422
District 15	4,071	1,500	36.84%	2,944,068
District 16	3,430	1,401	40.85%	2,838,196
District 17	3,885	574	14.76%	880,890
District 18	4,182	590	14.10%	991,824
District 19	4,279	672	15.70%	1,115,809
District 20	4,449	843	18.94%	1,458,688
District 21	4,469	843	18.86%	1,446,584
District 22	4,862	973	20.01%	1,622,905
District 23	3,527	713	20.20%	1,214,705
District 24	2,821	547	19.41%	973,338
District 25	4,135	570	13.79%	962,819
District 26	4,610	671	14.54%	1,151,962
District 27	4,630	663	14.32%	1,174,094
District 28	3,948	510	12.91%	865,661
District 29	3,949	596	15.10%	984,911
District 30	4,373	713	16.31%	1,218,579
District 31	3,388	1,291	38.10%	2,635,909
District 32	3,003	1,167	38.86%	2,337,019
District 33	3,934	641	16.28%	1,162,748
District 34	3,944	796	20.19%	1,452,176
District 35	4,280	679	15.86%	1,144,872
District 36	4,193	639	15.23%	1,106,459
District 37	4,627	610	13.18%	1,042,880
District 38	4,047	538	13.28%	908,825
District 39	4,022	571	14.19%	944,706
District 40	4,545	817	17.98%	1,380,415
District 41	2,890	1,208	41.80%	2,467,964
District 42	3,288	1,388	42.22%	2,960,211
District 43	4,455	644	14.45%	1,163,148
District 44	3,314	755	22.78%	1,293,620
District 45	3,685	636	17.27%	1,067,007
District 46	4,675	557	11.92%	997,722
District 47	4,450	600	13.48%	1,101,299
District 48	4,967	667	13.44%	1,225,439
District 49	4,918	964	19.60%	1,638,996
District 50	4,197	490	11.68%	808,989

House District	Total returns	EITC returns	% of Returns with EITC	EITC amt ($)
District 51	5,390	1,061	19.68%	1,797,715
District 52	4,270	650	15.22%	1,090,819
District 53	4,146	666	16.06%	1,121,203
District 54	4,644	788	16.96%	1,288,407
District 55	4,306	474	11.02%	779,454
District 56	4,310	471	10.93%	774,436
District 57	4,911	475	9.68%	806,675
District 58	4,079	531	13.02%	925,634
District 59	4,276	602	14.09%	1,006,255
District 60	4,185	497	11.88%	808,539
District 61	4,926	703	14.27%	1,051,962
District 62	4,313	674	15.63%	1,034,320
District 63	3,979	412	10.36%	498,999
District 64	5,453	591	10.84%	786,496
District 65	3,377	349	10.35%	408,075
District 66	6,009	632	10.51%	774,388
District 67	6,786	928	13.68%	1,493,815
District 68	4,765	685	14.38%	1,117,243
District 69	5,280	689	13.05%	1,105,718
District 70	6,301	706	11.20%	916,351
District 71	4,741	722	15.23%	1,175,843
District 72	3,945	643	16.30%	1,139,133
District 73	3,976	654	16.44%	1,109,627
District 74	3,286	550	16.73%	941,941
District 75	3,597	602	16.73%	1,031,112
District 76	3,956	662	16.74%	1,137,616
District 77	3,972	410	10.33%	678,162
District 78	4,448	725	16.31%	1,242,777
District 79	5,801	791	13.63%	1,242,357
District 80	4,399	598	13.60%	964,921
District 81	4,205	582	13.83%	901,959
District 82	4,190	567	13.52%	907,176
District 83	4,181	598	14.29%	1,022,478
District 84	3,959	540	13.65%	901,588
District 85	3,080	582	18.89%	915,905
District 86	4,016	663	16.50%	1,111,309
District 87	3,805	682	17.92%	1,171,843
District 88	4,726	865	18.30%	1,582,232
District 89	4,300	776	18.05%	1,378,674
District 90	4,234	642	15.17%	1,124,950
District 91	4,079	703	17.23%	1,069,291
District 92	4,081	734	18.00%	1,047,400
District 93	3,357	498	14.82%	737,794
District 94	4,654	665	14.29%	993,969
District 95	5,861	875	14.94%	1,287,575
District 96	4,279	693	16.20%	1,014,979
District 97	4,530	748	16.51%	1,098,968
District 98	5,431	865	15.93%	1,364,762
District 99	5,637	961	17.05%	1,362,970
District 100	4,439	687	15.48%	1,114,514

Source: Brookings Institute