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Congress has Critical Opportunity to Extend Targeted ARRA Tax Changes That Most Help Missouri Families

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THE EARNED INCOME TAX CREDIT (EITC): *Real help for working families*

Background

The Earned Income Tax Credit (EITC) has been helping low-income working families for over three decades. It is an efficient mechanism for putting cash back in the hands of millions of families who work hard, but earn low wages.

The EITC is calculated in three phases: during the phase-in stage the credit increases as a percentage of income; there is a flat amount for incomes with the ranges specified during the plateau phase; those with incomes above the range in the plateau receive the flat amount plus a percentage of income over that amount. The eligible amounts in each phase vary depending on the number of children in the family. The American Recovery and Reinvestment Act (ARRA) made two significant adjustments in the EITC.ⁱ

First, it drastically reduced the marriage penalty inherent in the EITC. Under the original law, low-income workers who married often found their EITC benefits reduced or completely eliminated. Steps were taken to improve this in 2001, by allowing couples to earn \$3,000 more in income than individuals, before starting the phase out. ARRA built upon this by allowing couples \$5,000 more in income than individuals.ⁱⁱ

ARRA also included additional EITC credits for larger families. EITC originally included different benefit levels, or tiers, for families with one child and families with two or more children. A third tier, for families with three or more children, was added in ARRA.

Both the marriage penalty relief and the help for larger families are set to expire in 2011.

What this means for families

Consider a couple planning to marry. Both work in low-income jobs and she has two children. If they do not marry, their combined EITC is \$5,156. Under the current law, if they marry, their combined EITC will be \$1,332. Should these provisions expire, and revert to the 2001 levels, their combined EITC will be \$910. And, if all marriage penalty relief expires, their EITC would be only \$279.ⁱⁱⁱ

- About 6 million people now benefit from marriage relief, including 11 million children.^{iv}

If the provision that increases benefits for larger families expires, each family would lose approximately \$629.

- Over 3 million families, with 13 million children, would be affected by this. **In Missouri, approximately 180,000 children would be affected if the third tier is not extended for larger families.**^v

What this means for economic stability

Families are the most fundamental unit of economic stability. Many families work hard, at low-wage jobs, to provide for their basic needs. The EITC allows these families to keep more of their income, stabilizing family finances so they can continue to contribute to the overall economy with their labor and spending. Continuing support for couples who choose to marry, and for children in larger families, is essential in tough economic times.

THE CHILD TAX CREDIT (CTC): *Real help for Missouri families with children*

Background

The Child Tax Credit (CTC) is a partially refundable credit for low- and middle-income working families. When first enacted in 1997, this credit was not refundable. In 2001, the credit became partially refundable for families earning over \$10,000. This \$10,000 threshold was indexed to inflation and, by 2007, had risen to \$12,000, even though wages did not rise at the same rate. This meant that fewer working families could claim the credit.

The threshold was lowered to \$8,500 in 2008 as part of the Troubled Assets Relief Program (TARP), and reduced again to \$3,000 for 2009 and 2010 as part of the American Recovery and Reinvestment Act (ARRA). Without legislative action, in 2011 the credit will no longer apply to earnings under \$12,850, when indexed for inflation.^{vi}

The maximum credit is worth \$1,000 per child. Higher income families may receive a reduced credit or be ineligible based on income. Working families earning too little to owe federal income tax receive 15 percent of the amount over the threshold, up to a maximum of \$1,000 per child.^{vii}

What this means for families

A mother with two children, working full time at minimum wage, earns \$14,500. Under the current law, she would receive a tax credit of \$1,750. If the threshold reverts to \$12,850, she would receive \$248.^{viii}

If we do not count earnings under \$12,850^{ix}:

- Low-income working families, including 7.6 million children, will lose their CTC entirely;
- More families, including 10.5 million children, will see a reduction, sometimes drastic, in the amount of their credit;
- The families that lose the most will be those with incomes between \$12,850 and \$16,333, including many families with a parent working full time for minimum wage;
- Families with incomes above \$10,000 would experience 80 percent of the losses;
- 600,000 children live in families with incomes that fall below the poverty line when they lose all, or part of this credit; families with 4 million children will fall further into poverty.

What this means for Missouri

An estimated 285,000 children will see a reduced CTC benefit if the threshold reverts to \$8,500^x

An estimated 325,000 children will see a reduced CTC benefit if the threshold reverts to \$12,850^{xi}

Extending the CTC changes is good for families and for the economy

- Parents who work full time, as cashiers, waitresses and in other service jobs, are able to support their families and achieve a basic standard of living with the CTC.
- This policy provides a strong incentive to work full time by increasing the credit as wages rise.
- The amount of additional credit most families will receive is just a few hundred dollars, but it makes a big difference for families struggling to get by in tough economic times.
- This credit is targeted to families who will spend the credit they receive on goods and services, increasing demand and stimulating the economy.

ⁱ Center on Budget and Policy Priorities, "Policy Basics: The Earned Income Tax Credit," retrieved from <http://www.cbpp.org/cms/index.cfm?fa=view&id=2505>, May 5, 2010.

ⁱⁱ Center on Budget and Policy Priorities, unpublished internal documents.

ⁱⁱⁱ Ibid.

^{iv} Ibid.

^v Ibid.

^{vi} Parrott, S., Sherman, A. & Huang, C., "Child Tax Credit Passed by Congress Will Help 13 Million Children," Center on Budget and Policy Priorities, October, 2008, retrieved from <http://www.cbpp.org/cms/?fa=view&id=283>, May 5, 2010.

^{vii} Ibid.

^{viii} Sherman, A., Feller, A. & Marr, C., "Failure to Extend Improvements in child Tax Credit Would harm Millions of Low-income Working Families," Center on Budget and Policy Priorities, February 16, 2010. Retrieved from <http://www.cbpp.org/files/2-16-10tax2.pdf>, May 6, 2010.

^{ix} Ibid.

^x Center on Budget and Policy Priorities, unpublished internal document.

^{xi} Sherman, A., Feller, A. & Marr, C., "Failure to Extend Improvements in child Tax Credit Would harm Millions of Low-income Working Families," Center on Budget and Policy Priorities, February 16, 2010. Retrieved from <http://www.cbpp.org/files/2-16-10tax2.pdf>, May 6, 2010.