The Earned Income Tax Credit: The Means Tested Welfare that Works

Maha Sadek

Follow this and additional works at: https://lawecommons.luc.edu/pilr

Part of the Civil Rights and Discrimination Commons, Criminal Procedure Commons, Environmental Law Commons, and the Human Rights Law Commons

Recommended Citation

Available at: https://lawecommons.luc.edu/pilr/vol23/iss2/5

This Article is brought to you for free and open access by LAW eCommons. It has been accepted for inclusion in Public Interest Law Reporter by an authorized editor of LAW eCommons. For more information, please contact law-library@luc.edu.
The Earned Income Tax Credit: 
The Means Tested Welfare that Works

Maha Sadek

The Earned Income Tax Credit (“EITC”) is a means tested “refundable tax credit for lower-income workers,” that was introduced in 1975.1 This article will focus on the federal EITC through a brief history, its current eligibility requirements, and the possibility of an expansion for childless workers.

BACKGROUND

Initially a small tax relief for low income workers,2 EITC was expanded under President Ronald Reagan “who deemed it ‘the best anti-poverty, the best pro-family, the best job creation measure to come out of Congress’.”3 In 1993, President Bill Clinton almost tripled EITC funding, an expansion due to his promise that that “full-time, year-round workers” who have dependent children could live above the poverty line.4 Jennifer Sykes, a Michigan State University professor who has done extensive research in EITC, notes that “the EITC’s steady expansion over time is strikingly important – it illuminates America’s commitment to the importance of encouraging work while also making strides to make work pay.”5 The popularity of EITC among politicians is evident in that “[e]ach administration prior to [Donald] Trump has expanded the EITC in significant ways.”6 In addition to the federal EITC, twenty-seven states and local governments enacted their own EITC that act as a supplement to the federal credit.7

---

2 Id. at 245.
3 Thomas Hungerford & Rebecca Thiess, The Earned Income Tax Credit and the Child Credit: History, Purpose, Goals, and Effectiveness, ECONOMIC POLICY INSTITUTE ISSUE BRIEF #370 1, 1 (2013).
4 Sykes supra note 1, at 244.
5 Email Interview with Jennifer Sykes, Assistant Professor at Michigan State University (Apr. 13, 2018).
6 Email Interview with Jennifer Sykes, Assistant Professor at Michigan State University (Apr. 13, 2018).
ELIGIBILITY

Eligibility for the EITC is dependent on the taxpayer’s income, number of children, and investment income.\(^8\) If the taxpayer earns under the pre-set limit, based on the number of qualified children\(^9\) they have (ranging from zero to three or more), the taxpayer is eligible to receive a tax credit.\(^10\) For example, for the 2017 tax year, a single parent with one qualifying child who earned less than $39,617, and had investment income less than $3,450, is eligible for EITC.\(^11\) The same eligibility requirements exist for married taxpayers, except that the income threshold increases to $45,207.\(^12\) The credit that is available to eligible taxpayers is based on a legislatively pre-determined range.\(^13\) All single parents with one qualifying child, therefore, will not receive the same amount of tax credit, but they all will receive a credit amount in the pre-set range.\(^14\) Eligible taxpayers with one qualifying child, for example, could receive a credit anywhere between $9 to $3,400.\(^15\)

The actual tax credit amount an individual taxpayer will receive within the range is calculated through a “phase in rate.”\(^16\) The phase in rate is a percentage, dependent on an individual’s number of qualified children and marital


\(^9\) Qualifying Child Rules, IRS (Sept. 20, 2017), https://www.irs.gov/credits-deductions/individuals/earned-income-tax-credit/qualifying-child-rules (stating a qualified child is a child with a SSN, it must be your “son, daughter, adopted child, stepchild, foster child or a descendant of any of them such as your grandchild,” or “brother, sister, half-brother, half-sister, step brother, step sister or a descendant of any of them such as a niece or nephew,” in addition to being under 19 (with some exceptions for full time students under 24), and if the child lives with the taxpayer in the United States for more than half the year).


\(^11\) Id. (Stating, qualification assuming other requirements such as having a SSN, filing taxes, you are a worker and have income of at least $1, and not filing Foreign Earned Income or Foreign Earned Income Exclusion).

\(^12\) Id. (Stating, the $45,207 income threshold only applies to married taxpayers who file joint tax returns).


\(^14\) Id.

\(^15\) Id.

status that is applied against the taxpayer's earnings. When the applicable phase in rate reaches the maximum EITC amount permitted, the phase in rate ends. Between the income level at which the maximum EITC amount allowed is met and a second predetermined threshold, the phase out rate, the maximum amount of EITC permitted is constant. For the 2016 tax year a single taxpayer who had two qualifying children and made less than $44,648 was eligible for EITC. If the taxpayer made between $13,390 and $18,190, the EITC credit was constant, and they received the maximum credit amount of $5,572. If, however, the taxpayer made less than $13,390, the phase in rate would apply, and the EITC credit received would be determined by calculating 40% of the taxpayer’s earnings. If the taxpayer earned more than the second threshold ($18,190) during the taxable year, the phase out period begins. The phase out period decreases the EITC credit by a pre-set phase out rate. The phase out rate is applied until the taxpayer's earnings exceed the phase out threshold, and their EITC credit is reduced to zero.

WHY EITC IS A SUCCESSFUL PROGRAM

Based on the 2016 taxable year, “almost 27 million taxpayers received over $65 billion in EITC.” The 2014 national participation rate for EITC is 80%, with no individual state’s participation rate falling below 71%.

Researchers have found that EITC is more successful than other means tested programs for several reasons. First, EITC refunds are delivered through

---

17 Id. (Note the difference in the maximum tax credits in Table 1 varies from the max tax credits initially cited in this article because Table 1 relied on 2016 rates and the rates above are 2017 rates).

18 Id.

19 Id.

20 Id.

21 Id.

22 Id.

23 Id.

24 Id.

25 Id.


28 Sykes, supra note 1 at 244.
the IRS, a universal system used by all taxpayers. Second, EITC receives bipartisan support since it targets a “valued group—working parents.”

Because the EITC is distributed through the IRS and eligibility is determined through individual workers’ tax returns, the stigma that typically surrounds means tested welfare does not exist. The recipients of EITC are not distinguished from other taxpayers in any way. The credit is applied through a tax refund check, a check that many taxpayers, not just poor taxpayers, receive. Furthermore, every taxpayer encounters the IRS yearly. There is not a specialized office or system for low income taxpayers to encounter. The lack of stigma encourages taxpayers to take advantage of EITC, making the program more successful than other means tested welfare. When one taxpayer who had to turn to Temporary Aid for Needy Families (“TANF”), another means tested welfare program, she noted that using TANF made her feel like “crap,” and that the money she received was not “really worth it.” While discussing her EITC refund, however, the same taxpayer noted that she thought about the credit all year long, and that the check “fueled her dreams.” The stark difference in the taxpayer’s perception of EITC is common, and likely why EITC receives bipartisan support while other means tested social programs do not.

Democratic and Republican politicians, including Presidents Reagan, Obama, Clinton, and Speaker of the House of Representatives Paul Ryan, have endorsed EITC. EITC receives bipartisan support because it encourages taxpayers to work. Unlike other means tested programs, the amount of EITC credit possible increases the more the taxpayer earns, until the maximum amount is reached. Because these taxpayers are working, the public views the credit not as welfare, but as a way to “lift up those who are seen as keeping up

29 Id.
30 Id.
31 Id. at 257.
32 Id.
33 Id.
34 Id.
35 Id. at 260.
37 Id.
38 Id.
39 Id.
41 Id.
their end of the social contract.” This view is reiterated through the public and government’s references to the EITC. EITC is never referred to as welfare; the IRS calls the EITC a “financial boost for families.” It is seen as a tax “refund,” and recipients are not categorized as “takers.”

**BENEFITS OF THE EITC**

In 2015, the EITC “lifted about 6.5 million people out of poverty, including about 3.3 million children.” The number of poor children would have been more than one-quarter higher without the EITC. In addition, the credit “reduced the severity of poverty for another 21.2 million people, including 7.7 million children.” The EITC gives families the opportunities to pay off or decrease debts, build assets, and supplement current consumption expenses.

Additionally, the benefits derived from the EITC go beyond the year the credit is received. Women who have received the EITC experienced “higher wage growth in subsequent years than otherwise-similar women who did not benefit. [As a result, the] EITC boosts the size of the Social Security retirement benefits they ultimately will receive.” Furthermore, children of low-income families, who receive the EITC and other related children tax credits, “do better in school, are likelier to attend college, and likely earn more as adults; they also are likelier to avoid the early onset of disabilities and other illnesses associated with child poverty,” in comparison to children in low-income families who do not receive EITC.

---

42 Halpern-Meekin et al., supra note 36.
44 Halpern-Meekin et al., supra note 36.
46 Id.
47 Id.
50 Id.
CHILDLESS WORKERS

Several tax code provisions, through standard deductions and personal exemptions, ensure that individuals with dependent children are not subject to income tax until their earnings exceed the poverty line. These protections, in addition to the benefits received of the EITC, are not available for childless workers. Childless workers below the poverty line are taxed further into poverty because they are subject to income tax while their earnings are below the poverty line, receive little to no EITC, and are subject to payroll taxes.

A single childless worker becomes ineligible for any tax credit when they earn above $15,010. The federal minimum wage is $7.25 per hour, meaning that any childless worker who works full time (40 hours per week) and is paid minimum wage is ineligible for the EITC. These individuals are taxed between a 10% or 12% rate based on their income, in addition to payroll taxes. An individual’s share of payroll taxes, which includes Social Security and Medicare taxes, is 7.65% of earnings. A single childless worker who works 35 hours a week and is paid $7.25 an hour, is subject to a $986 tax

---

52 Id.
53 Id.
56 40 hours per week x $7.25 per hour= $290. $290 per week x 52 weeks in a year= $15,080. $15,080 of earned income is greater than the $15,010 threshold for childless workers to receive EITC.
liability. They are eligible for $184 in EITC, but this amount is so minimal that it does little in comparison to their total tax liability.

Politicians on both sides of the aisle have recognized the issues with taxing childless workers further into poverty, and three main proposals currently dominate the discussion for a solution. The Baseline proposal is a combination of President Obama’s FY 2016 budget proposal and Speaker Ryan’s anti-poverty blueprint. This plan doubles the maximum credit and expands income and earnings eligibility to 125% of full time work at the federal minimum wage. The Moderate proposal is modeled after congressional proposals; it triples the credit and expands income and earnings eligibility to 133% of full-time work at minimum wage. Finally, Generous proposal tripled the maximum credit, and expands income and earnings eligibility to 175% of the full time minimum wage.

Proponents of these three proposals provide “tradeoffs” that would cut spending under an EITC expansion for childless workers. The biggest tradeoffs include student restrictions and hours worked requirements. Currently, EITC is limited to individuals over the age of twenty-five. Propositions have been made to expand age eligibility to individuals over the age of twenty-one. This expansion would pose issues of increased cost and college student identifi-

60 Chuck Marr & Bryann DaSilva, Childless Adults Are Lone Group Taxed Into Poverty, CENTER ON BUDGET AND POLICY PRIORITIES, (Apr. 19, 2016), https://www.cbpp.org/sites/default/files/atoms/files/3-2-16tax.pdf. (This includes payroll taxes and income tax. How her tax liability is determined: “[S]he will claim a $6,300 standard deduction and one personal exemption of $4,050 for a combined $10,350. Subtracting this amount from her income leaves $2,144 in taxable income. She is in the 10 percent bracket so will have a $214 income tax liability.” Add income and payroll taxes = $1,170 - $184 EITC = $986 tax liability).
61 Id.
63 Id.
64 Id.
65 Id.
66 Id. (“The generous option is loosely based on the New York City demonstration project (Paycheck Plus) . . . The generous option was also loosely based on the Brookings Institution’s proposal”).
67 Id. at 10.
68 Id.
69 Id. at 5.
70 Id. at 10.
cation. The age expansion would result in a multi-billion dollar cost increase under each of the three proposals.

In addition to the increased cost, the age expansion would make most college students eligible for EITC. This is problematic because some students who appear to be in need of government assistance may, in reality, financially rely on affluent parents or guardians. The IRS would face difficulty in determining if a student is truly in need of assistance or is filing taxes independently to receive this tax benefit. A student exclusion could be applied, but this raises issues of student identification. The IRS is aware of student status when colleges file an expense form, 1098-T form, with the IRS. This is not sufficient, however, as "educational assistance (Pell Grants, scholarships, and so forth) is not reported on a 1098-T, which means that students who have no out-of-pocket education expenses will not be flagged as a student to the IRS." While excluding students could save billions of dollars under each plan, the complicated nature of student identification makes the exclusion unlikely.

The other proposed tradeoff is imposing a number of weeks worked or hours worked per week requirement. The purpose of this tradeoff is to limit taxpayers who "who work only a few weeks a year for high wages and salaries." Because no tax forms include the number of hours or weeks worked, this requirement is difficult to enforce. Some proponents have suggested enforcement by ensuring that taxpayers "with earnings less than half-year work at minimum wage ($6,600) would not be eligible for the childless worker EITC." This enforcement mechanism, however, does not completely address the problem of workers who could earn most of their income through a few weeks of work. In theory, this additional requirement saves the federal gov-

71 Id.
72 Id.
73 Rachidi, supra note 62.
74 Id.
75 Id.
76 Id.
77 Id.
78 Id.
79 Id.
80 Id.
81 Id.
82 Id.
83 Id.
84 Id.
ernment billions, but due to the lack of methods available to track hours worked, proves too difficult to apply.85 If the age restriction and work requirements could be effectively applied, they could act as tradeoffs for expanding EITC to childless workers.86 If the bipartisan effort to increase EITC funding continues, we may see an eventual increase in the EITC for childless workers. With growing polarization and increased federal budget disagreements that most recently led to a government shutdown, it is hard to imagine Congress approving such a large expansion to the EITC, even if the tradeoffs were within reach.87 Jen Sykes states that though the present administration is unwilling to expand the EITC at all, let alone for childless workers, she remains cautiously optimistic, noting that EITC is “an effective policy tool to decrease poverty in this population that often falls through the cracks in our safety net.”88

85 Id. at 11.
86 Id. at 13.
88 Email Interview with Jennifer Sykes, Assistant Professor at Michigan State University (Apr. 13, 2018).