

Making Work Pay and Making Ends Meet

How Iowans Gain from Child Tax Credit and Earned Income Tax Credit

Even in today's charged political climate, most agree that someone working full time should not be poor. The Earned Income Tax Credit (EITC) has received broad bipartisan support in its 30-plus year history, because it encourages and rewards work.¹ The more a lower-income worker earns, the larger the credit available, to a point.² In 1997, Congress added the Child Tax Credit (CTC), which provides low- to middle-income parents with a tax credit that recognizes the cost of raising children and that also rewards work.³

Since their creation, both the EITC and the CTC have been improved and expanded, providing more working families with a larger credit. Most recently, the 2009 Recovery Act⁴ improved both credits.

The value of both credits rises with earnings, and then begins to phase out. Both credits are refundable, so if a family's EITC and CTC exceed their tax liability, they will receive a refund check. This assures stability for the family's budget, and helps the economy as well. Because these credits put more cash into the wallets of the lowest-income Americans, the money quickly re-enters the state and local economy, preserving and creating jobs for other workers.

As the lame-duck Congress faces decisions about the expiring 2001-03 Bush tax cuts, it should consider the impact of the Child Tax Credit and the Earned Income Tax Credit improvements. If these improvements expire at the end of the year, fewer dollars would pass through to the lowest-earning workers and there would be greater need for public assistance for their families.

Recent Improvements to the Credits

Both the CTC and EITC increase in value as an individual earns more. The CTC has a maximum value of \$1,000 per child. Tax law changes in 2001 made substantial improvements to the CTC, followed by Recovery Act improvements in 2009 that allowed the CTC to begin accruing when income reaches \$3,000, meaning more of the lowest-earning workers could qualify. Under the previous rules that will take effect if the Recovery Act and the 2001 improvements expire, the CTC will begin accruing only on income above \$12,850. A single parent with two children working full time at the minimum wage would see his or her CTC slashed from \$1,725 to \$250 if the improvements lapse. That's a loss of \$1,500 in spendable income for someone earning \$14,500 a year and raising two children.

The EITC also helps the lowest-income parents, and is even more highly targeted. The Recovery Act improved the EITC by creating another tier for parents with three or more children and reducing the effect of a marriage penalty. Two persons who qualify for the EITC see a reduced benefit if they marry, which the Recovery Act took steps to ease. Under the old EITC rules, the EITC began to phase out for married couples at a level \$3,000 higher than for single workers. The Recovery Act increased the phaseout threshold to \$5,000.

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For example, consider a single parent of two making \$15,000 and a companion making \$25,000 a year. If they remain single, their combined EITC is \$5,156. If they marry, their combined EITC is \$1,332 under the current rules — about one-fourth of the pre-marriage benefit. If the Recovery Act improvements expire the couple’s EITC would fall from \$1,332 to \$910. If the 2001 marriage penalty relief expires as well, the couple’s EITC would fall to \$279.

How the Credits Help Iowa Families

In Iowa, extending these improvements would provide significant aid to families with the lowest income. On average, these credits would combine to provide the lowest 60 percent of earners with a \$44 tax cut. The lowest 20 percent of earners would see an average tax cut of \$50, and the next-lowest 20 percent would see an average combined tax cut of \$75.⁵

Table 1 provides further information on the number of Iowa families and children who would benefit from an extension of the Recovery Act improvements to both credits and the number of Iowa families and children who would see a larger credit. Some families and children become newly eligible for the EITC and Child Tax Credit, while other families currently eligible receive greater benefits. Altogether, more than 50,000 Iowa families and 150,000 children benefit.

Table 1. Thousands of Iowa Families and Children Benefit from Improvements to Child Tax Credit and Earned Income Tax Credit

| | Earned Income Tax Credit | | | Child Tax Credit | | |
|----------|--------------------------|------------------------------------|--|-----------------------------|----------------------------|--|
| | Current law | Recovery Act improvements extended | Families with bigger credit from extension | \$12,850 earnings threshold | \$3,000 earnings threshold | Iowans with more credit from lowered threshold |
| Families | 128,083 | 155,357 | 55,836 | 306,568 | 324,052 | 52,135 |
| Children | 237,687 | 261,268 | 155,017 | 587,023 | 615,286 | 103,716 |

Source: [Citizens for Tax Justice, “Refundable Tax Credits Expanded in the Economic Recovery Act”](#)

Maintaining the Earned Income Tax Credit and the Child Tax Credit improvements would help thousands of the lowest-earning Iowans, and also help the economy by putting more money into the hands of low-earning families who need to spend the money quickly.

¹ Steve Holt, “The Earned Income Tax Credit at Age 30: What We Know,” Brookings Institution. February 2006. <http://www.brookings.edu/~media/Files/rc/reports/2006/02childrenfamilies_holt/20060209_Holt.pdf>.

² For more background information on the Earned Income Tax Credit, see “Policy Basics: The Earned Income Tax Credit,” Center on Budget and Policy Priorities. December 4, 2009. <<http://www.cbpp.org/cms/index.cfm?fa=view&id=2505>>.

³ For more background information on the Child Tax Credit, see “Tax Credit with Lasting Benefit,” Iowa Fiscal Partnership, June 14, 2010. <<http://www.iowafiscal.org/2010docs/100614-IFP-CTC-bgd.pdf>>.

⁴ American Recovery and Reinvestment Act, also known as ARRA.

⁵ Citizens for Tax Justice, “Refundable Tax Credits Expanded in the Economic Recovery Act,” October 19, 2010. <<http://www.ctj.org/pdf/arracredits.pdf>>.

Iowa Fiscal Partnership

The Iowa Fiscal Partnership is a joint initiative of the Iowa Policy Project and the Child & Family Policy Center, two nonprofit, nonpartisan Iowa-based organizations that cooperate in analysis of tax policy and budget issues facing Iowans. IFP reports are at <http://www.iowafiscal.org>. IFP is part of the State Fiscal Analysis Initiative, a network of state-level organizations and the Center on Budget and Policy Priorities to promote sound fiscal policy analysis. IFP work is supported by the Stoneman Family Foundation and the Annie E. Casey Foundation.