



Grantmakers
for Children,
Youth & Families

EITC
Funders Network

GIST
Grantmakers Income
Security Taskforce

research

policy

practice

Insight

Fall 2015



Two Generation
Approaches to
Poverty Reduction
and the EITC

A Review of Current CYF Topics and Issues



About Us

Grantmakers for Children, Youth and Families (GCYF), established in 1985, is a membership association of grantmaking institutions and is headquartered in the Washington, D.C. area. GCYF is the leading authority and resource for funding organizations dedicated to ensuring informed grantmaking that best supports positive, long-term outcomes for children, youth, and families. GCYF convenes and engages diverse constituencies in its network of local, regional and national grantmaking organizations across the country—including trustees, executive directors, vice presidents, and program officers and associates. GCYF provides comprehensive research, resources and knowledge-based insight and perspective in its ongoing support of member organizations. GCYF serves as a forum to review and analyze grantmaking strategies, exchange information about effective programs, examine public policy developments and maintain ongoing discussions with national leaders. We value the integration of research, policy and program grantmaking strategies, which address the complex needs of children, youth, and families. For more information, visit www.gcyf.org.

The EITC Funders Network brings together funders interested in the Earned Income Tax Credit, free- and low-cost tax preparation, and asset building. The EITC Funders Network seeks to provide a platform for discussion and exchange among funders and disseminate information based on field-wide issues and concerns. As a result of our work, funders are more informed about EITC-linked strategies to reduce poverty, able to shape the field according to emerging best practices and collaborate more effectively with each other and their grantees. For more information, visit www.eitcfunders.org.

Grantmakers Income Security Taskforce (GIST) is a national network of grantmakers interested in improving economic well-being of low-income families in the United States. Established in 1992, GIST operates as an umbrella group for participating funders and philanthropic advisors, providing a neutral forum for strategic discussion and acting as a vehicle to encourage co-investment among foundations and facilitate cooperation among grantees on high priority issues. Collectively, GIST members have provided the vast majority of non-governmental support for the nation's efforts to reform welfare and income security policy over the last decade. For more information, visit www.gistfunders.org.

Insight

FALL 2015

What's Inside

4

Introduction

By La June Montgomery Tabron, W.K. Kellogg Foundation

6

Poverty and Inequality in America: Why We Should Care and What We Should Do

By Indivar Dutta-Gupta and Kali Grant, Georgetown Center on Poverty and Inequality

12

Overview of the Earned Income Tax Credit

By Robert Greenstein, Center on Budget and Policy Priorities

16

Using the Earned Income Tax Credit to Encourage Work and Increase Income from Work

By David Neumark, University of California, Irvine, National Bureau of Economic Research and Institute for the Study of Labor

22

Earned Income Tax Credit and Educational Outcomes

By Gordon B. Dahl, University of California San Diego

25

The Earned Income Tax Credit's Impact on Health

By Peter S. Arno, PhD and Jeannette Wicks-Lim, PhD, Political Economy Research Institute, University of Massachusetts, Amherst

29

Earned Income Tax Credit, Savings and Child Outcomes

By Don Baylor, Urban Institute

33

The Earned Income Tax Credit and Community Economic Stability

By Natalie Holmes and Alan Berube, Brookings Institution

36

Conclusion

By Patrick McCarthy, The Annie E. Casey Foundation

39

Acknowledgments

Introduction

By La June Montgomery Tabron, W.K. Kellogg Foundation

Anyone who wonders whether a well-crafted government policy can improve life for working, lower-income Americans should take a look at the Earned Income Tax Credit (EITC).

In terms of poverty reduction, the EITC does precisely what most Americans expect such a policy to do: encourages and rewards work, and creates a financial incentive for people to leave public assistance and remain employed. The EITC also encourages low-wage workers to increase their work hours as to take greater advantage of EITC benefits.

In the 2013 tax year, more than 27-million Americans received the federal EITC, which comes to recipients as an Internal Revenue Service (IRS) tax-refund check. The average EITC payment in 2013 was \$3,074 for a family with children and an income of \$25,000. For a single mother with an income between \$13,000 and \$18,000, EITC can provide up to \$5,000 of extra income. That's equivalent to a \$2.60-per-hour pay raise. It's no wonder that the EITC has become the nation's most effective antipoverty policy. In 2013, it lifted some 6.2-million families out of poverty.

All this stems from a program whose benefits few would call exorbitant. Yet we shouldn't underestimate how even \$2,000 extra per year can buffer low-wage workers from what one writer in this issue calls "the vicissitudes of life" — in other words, the car repairs and other necessities that can imperil families with scant room in their budgets to cover emergencies.

"The EITC helped me pay down some of my bills and it's really been a financial blessing. I've saved for my children. I haven't saved for myself. Things are coming at me left and right so it makes it real hard to save for anything I want. It's about my children."

—Mother of two school age children living in the Midwest

Further, as the compelling essays that follow make clear, the EITC's impact extends well beyond the financial. Since the program began in 1975, research shows that EITC helps adults and children in multiple areas across the life span:

- Mothers who receive EITC are less likely than other low-income mothers to smoke before and after pregnancy, and more likely to eat healthy diets and deliver babies at healthy birthweights.

- Children in EITC families score better on math and reading tests than low-income children in families who do not receive the EITC and are more likely to finish high school and attend college.
- Children from EITC families, on average, go on to earn 17% more when they reach adulthood than do children from low-income families who do not receive the EITC.
- Workers who receive EITC boost their Social Security retirement benefits, which can reduce the severity of poverty in old age.
- Families that receive EITC (some 95%) use large portions of the refund to pay down debt or cover deferred expenses such as car repairs.

The EITC's great versatility offers a wealth of creative program opportunities for funders. This is especially true with two-generation approaches that serve adults and children simultaneously. Two-generation strategies to leverage the EITC could include income security, education, health, workforce development, and more.





There's no need, though, for new or established funders to go it alone. There's much to gain from our common experience. The Kellogg Foundation has benefited from its membership in the EITC Funders Network. The network's 275-plus members consist of funders who work at the national, regional, and local level. Network members can collaborate on funded projects, and through meetings and conference calls receive updates from leading EITC policy experts.

One outgrowth of a collaboration between the EITC Funders Network and the Grantmakers Income Security Taskforce has been the EITC Rapid Response Fund. The fund provides much-needed communications assistance to state advocacy and community groups who provide educational materials that inform the public and policymakers about the value of the


EITC. This funding has been critical as threats to the EITC mean that ten-of-thousands of low-income families stand to lose millions of dollars in support. These efforts are essential, as 26 states and several municipalities have established EITCs that build on the federal program.

There's also much we can do as funders to increase participation in this time-tested program. One way is to encourage other nonprofits and faith groups to receive the Volunteer Income Tax Assistance (VITA) training and equipment offered free by the IRS.

The volunteer tax preparers trained by VITA help eligible citizens complete their EITC applications. (Given the form's complexity, most filers would otherwise have to pay a commercial tax preparer.) In 2014, VITA sites served over 3.2 million filers who received \$3.9 billion in refunds. Other potential VITA partners include municipalities and retailers, who know that EITC recipients spend a large portion of refund monies in their communities.

Support for more VITA sites could also increase the number of new EITC enrollees. Currently, some 21% of eligible taxpayers have not applied for the program. With targeted action to spur new EITC sign ups, we could make a substantial economic difference for tens of thousands of working families with children.

We know that the EITC's wide reach offers ample room for funders to build on its success. The papers that follow explore some of these possibilities. As just one example, more VITA sites could become hubs where families can use their "tax-time moment" to enroll in savings programs for education or retirement. New York and Texas already support such initiatives.

The EITC is the nation's largest antipoverty program and has been widely acclaimed as one of the most successful. There's no need for funders to reinvent this particular wheel if they want to help children thrive in school and life. Instead, we can support efforts that make the EITC larger, stronger, and better able to do what it's done so well for 40 years: make work pay for those families who need it the most. 

Poverty and Inequality in America: Why We Should Care and What We Should Do

By Indivar Dutta-Gupta and Kali Grant, Georgetown Center on Poverty and Inequality

Introduction

Persistent poverty and rising inequality conflict with our nation's values and threaten our future. If poverty or inequality don't trouble you, growing evidence suggesting that they limit opportunity and our nation's economic prosperity should. This reality also means that efforts to address the separate but related challenges of poverty and inequality can simultaneously expand economic security and opportunity while growing the economy. At the same time, persistent poverty and extreme inequality can be attributed in large part to the choices we make to shape our economy and opportunity structure (Stiglitz, 2015).

A number of barriers stand in the way of building the will for implementing a policy agenda that addresses these challenges. First, the public significantly underappreciates the extent of these problems (Fitz, 2015). In addition, new research suggests that *perceptions* of inequality appear to be more strongly correlated with policy responses than *actual* levels of inequality (Gimpelson & Treisman, 2015). Spreading information about inequality and poverty alone, however, will be insufficient—as other research finds that the distrust of government limits the willingness to support appropriate public policy solutions, especially solutions that involve the tax and transfer system (Kuziemko, Norton, Saez, & Stantcheva, 2015). That same research does suggest that some people can be persuaded by highlighting the tangible effects of specific policies.

We don't have to persuade everybody, but the tasks are clear for those of us who fight for low-income and disadvantaged children and families: Communicate clearly the nature of the problems, offer proposals that support our nation's values and future prosperity, and engender public confidence in our solutions.

Successful two-generational poverty- and inequality-reducing initiatives, including the Earned Income Tax Credit (EITC) and early care and education, connect with deeply held tenets of freedom, family, work, and community, and allow advocates to tell compelling stories that can build the public and political will we need (Center for Community Change, 2014). Below, we share key facts and offer a framework for communicating about and addressing poverty and inequality by highlighting specific efforts that help disadvantaged children and families.

Poverty and Inequality in America

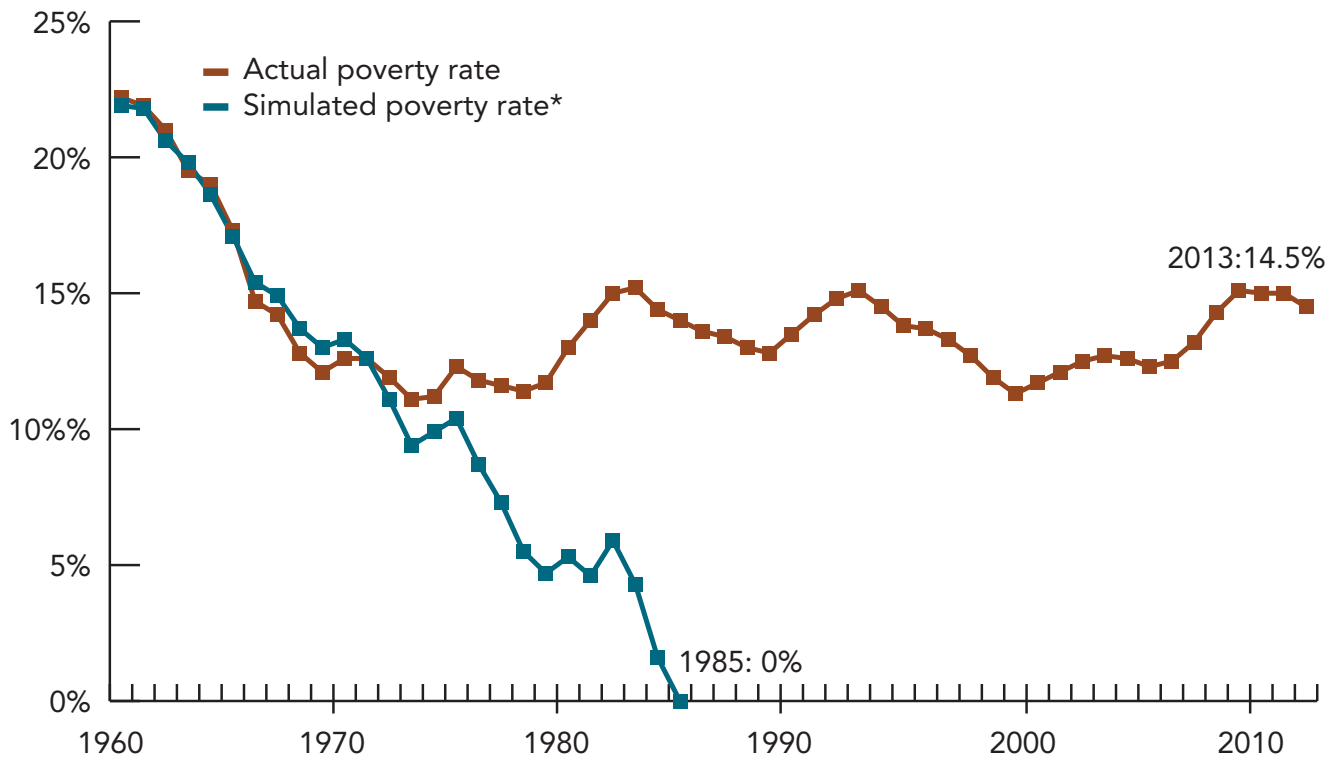
Poverty typically refers to a floor for economic resources or material deprivation, below which nobody should fall. While the poverty measure in America is not adjusted to account for such changes over time, most of us likely would set that floor in some relation to prevailing living standards. Adam Smith's *Wealth of Nations* (1904) cited the lack of a linen shirt—something that did not exist in earlier times—as evidence of poverty in 18th-century Europe. In this sense, poverty may seem to be a component of inequality, though it is the idea of a minimum floor that is core to the concept of poverty. In contrast, inequality typically refers to the distribution of economic resources throughout the population and does not on its own refer to a particular floor or ceiling, though raising floors (and lowering ceilings) would of course reduce inequality.

In 2014 (the most recent year for data), 14.8% of the population had low enough pre-tax cash income to be considered poor under the Official Poverty Measure (U.S. Census Bureau, 2014). More than one in five (21.1%) children lived in poverty (DeNavas-Walt & Proctor, 2014). Even under the more comprehensive Supplemental Poverty Measure that counts taxes, tax credits, and cash-like benefits against a less meager poverty threshold, the poverty rate was 15.3% overall and 16.7% for children (Short, 2014).

Alongside poverty, income and wealth inequality persists at virtually unprecedented extremes not seen since just before the onset of the Great Depression (Saez & Pikkety, 2015 and Saez & Zucman, 2014). The growing concentration of economic resources among the more affluent and away from those with limited means during the past half century contributed four times more to poverty than changes in family structure and racial composition in the American population, according to the Economic Policy Institute (Gould, Davis, & Kimball, 2015). Indeed, had economic growth continued to produce shared prosperity as it had from 1959 to 1973, official income poverty would have come close to elimination decades ago (Danziger, 2007). In addition, in recent years, nearly all but the wealthiest have been left out from the economic recovery—for example, in the first three years of the recovery, incomes of the top 1% increased by 34.7%, while the bottom 99% incomes only grew by 0.8%, meaning that from 2009 to 2012, 91% of all economic gains went to the top 1% (Saez, 2015).



Figure 1: Poverty rate, actual and simulated, 1959–2013



* Simulated poverty rate is based on a model of the statistical relationship between growth in per capita GDP and poverty that prevailed between 1959 and 1973.

Source: EPI analysis of Current Population Survey Annual Social and Economic Supplement *Historical Poverty Tables* (Tables 2 and 4), Bureau of Economic Analysis National Income Product Accounts public data, and Danziger and Gottschalk (1995)

Race and Gender Are Intertwined with Poverty and Inequality

Poverty and inequality have important racial and gender dimensions, fueled by structural disparities in criminal justice, pay, and education that cannot be ignored. By 2043, we will have a “majority minority,” and yet, we continue to leave behind kids of color who will be a growing share of the future workforce (Mather & Jarosz, 2014). In 2013, racial and ethnic minorities had a poverty rate that was 13 percentage points higher than that of non-Hispanic Whites (Mather & Jarosz, 2014). Researchers estimate that had we not chosen our devastating path of mass incarceration, poverty rates would be 10% to 20% lower overall, with larger improvements for communities of color (Defina & Hannon, 2013).

In terms of gender disparities, women are still 32% more likely to be poor than men (Casey, 2014). For women of color, the odds are even worse (Casey, 2014). Single female-headed families with children are also much more likely to be poor than single male-headed families with children. For female-headed

families of color with children, poverty is even more pervasive, with nearly half of all African American and Hispanic families, and over half of all Native American families, living in poverty (Gallagher Robbins & Morrison, 2014). Ensuring equal pay for women would slash the poverty rate in half among working women (from 8.1% to 3.9%), and by nearly half among working single mothers (from 28.7% to 15.0%; Hartmann, Hayes, & Clark, 2014).

In 2013, White families had, on average, six times the wealth of Hispanic families and seven times that of African American families (Urban Institute, 2015). Income and wealth gaps mean these families have significantly fewer resources to invest in themselves, their children, and their communities. For example, African American families have to wait an average of eight years longer than White families to purchase a home (Mather & Jarosz, 2014). Despite significant progress in shrinking the Black-White achievement gap, college attainment rates continue to reflect significant racial (and income) disparities (The Stanford Center on Poverty & Equality, 2014). And though

higher education typically leads to greater incomes and wealth accumulation, it is less helpful for Latinos and African Americans (Emmons & Noeth, 2015).

Poverty and Inequality Create Economic Disadvantage

By creating economic disadvantage, both poverty and inequality limit the life chances of a large share of our population. With each passing decade, we uncover new knowledge about the far-reaching harm—for children, families, and society—of this economic disadvantage. We've long known that insufficient family resources are strongly associated with material hardship (Dutta-Gupta, 2011). Research has also confirmed that childhood poverty hinders school achievement, harms health, increases interaction with the criminal justice system, and worsens labor market outcomes in adulthood (Children's Defense Fund, 2015). More recently, we have learned about stress from poverty affecting brain development and a range of cognitive and non-cognitive skills (Kautz, Heckman, Diris, ter Weel, & Borghans, 2014), and that even growing up in a high-poverty neighborhood significantly lowers one's chances for upward mobility (Chetty & Hendren, 2015). Such high social costs of poverty and inequality have real, economic consequences for all of us. Research from the Organisation for Economic Co-operation and Development (OECD) suggests that rising inequality in wealthy nations reduces economic output by depressing educational outcomes for disadvantaged children (Cingano, 2014). In the U.S., costs associated with persistent childhood poverty alone amount to almost 4% of our GDP—hundreds of billions of dollars—each year (Holzer, 2010). International Monetary Fund (IMF) research similarly



indicates that raising incomes for those with low incomes increases economic growth, while greater incomes for the wealthiest reduces growth (Dabla-Norris, 2015). In addition, IMF research suggests that economies with less inequality have longer economic expansions than more unequal societies (Berg & Ostry, 2011).

What Do We Do About It?

We have also gotten smarter about how we address the complexities of economic disadvantage created by poverty and inequality. We can say confidently that we have at least partial—often cost-effective—remedies at each step from before birth into adulthood (Dynarski, Hyman, & Whitmore Schanzenbach, 2011). Below, we highlight a number of policies organized by four key pillars for a multigenerational strategy to reduce poverty and inequality, offering a glimpse of the array of effective approaches to addressing these challenges. In particular, we consider how the EITC, in conjunction with other programs and policies, can help meet immediate needs while promoting long-term benefits for the most vulnerable children and families.

Empower Disadvantaged Groups in Our Political System

Mitigating poverty and inequality requires an explicit focus on empowering disadvantaged groups and eliminating racial, gender, sexual orientation, and other forms of invidious discrimination. Broad measures such as comprehensive immigration reform would normalize the status of more children and workers and increase their educational and work opportunities. Democracy must also become more representative (Dutta-Gupta, 2015), as political science research confirms what many of us have feared: in policy disagreements between the most well-off and everyone else, the wealthy consistently win (Gilens, 2014). Strengthening and protecting the Voting Rights Act, leveling the playing field for political contributions, and limiting the influence of corporate lobbyists are all key tasks. We must also prevent further disenfranchisement of especially vulnerable groups by restoring and increasing access to legal aid and reversing over-incarceration and over-criminalization. If people have a voice in the political and judicial systems, they will have a real chance in our economic system.

Ensure Good Jobs and Economic Security for All Workers

Thanks to minimal wage growth, deteriorating job quality, and limited worker protections, hardworking families still struggle to get ahead. Reaching full employment, both by investing in physical infrastructure (including transportation, water, and affordable housing) and other national needs and by increasing employment opportunities through subsidized jobs, is one of the most effective strategies we can pursue to help the working and middle class (Baker & Bernstein, 2013). Unions can also promote economic mobility for low-income children in the U.S., with an area's union density among the strongest predictors



of upward mobility (Freeman, Han, Madland, & Duke, 2015). Even when jobs are plentiful, labor standards help ensure job quality. Raising the national minimum wage, requiring fair scheduling for workers, fighting employee-contractor misclassification and wage theft, and enacting the Paycheck Fairness Act to address the gender wage gap would also help push back on poverty and inequality.

Strengthening the EITC is another core strategy. Recent research finds that a more complete accounting of the EITC's impact in boosting employment and incomes reveals a far larger antipoverty effect than previously understood (Hoynes & Patel, 2015)—not to mention the tax credit's secondary benefits for health and education, including child test scores and the likelihood of attending college (Marr, Huang, Sherman, and DeBot, 2015; Sherman, Trisi, & Parrott, 2013). And when income does come in, workers need protection and empowerment through stronger consumer financial protection rules, access to mainstream financial institutions, and the right savings vehicles.

Help People Prepare for Work and Meet Family Responsibilities

Opportunities for education and training for good jobs should be accessible and affordable for everyone at every stage of life. Universal early learning and quality education through grade school and beyond help lay the groundwork for success in adulthood (Reynolds, 2015). Increasing funding for public schools serving poor children significantly reduces intergenerational poverty (Jackson, Johnson, & Persico, 2014). All individuals deserve the chance to get ahead through higher education without debt, and when there must be debt, income-based repayment should be an option.

Policies and programs that provide families with more tools to manage their many responsibilities will benefit parents and other adults immediately, while aiding children even more in the long run. Providing paid family and medical leave (National Partnership for Women & Families, 2015), home visitation (Avellar et al., 2014), affordable child care, and comprehensive family-planning services, as well as increasing incomes (Dahl & Lochner, 2012) for disadvantaged families through a child allowance will promote equity and security by ensuring that all women and families are able to maintain steady work and much needed income while having more control over their lives (Boonstra, 2008).

Insure Against the Vicissitudes of Life

People often cannot work or earn enough to meet basic needs, making a strong safety net essential. In 2013, work supports and public insurance (both contributory and noncontributory) programs lifted 40 million people out of poverty (Sherman, Trisi, & Parrott, 2013). Still, gaping holes in the safety net call for repair (Edelman, 2014). Addressing flaws in Temporary Assistance for Needy Families (Dutta-Gupta & Grant, 2015) to



refocus it on employment and child well-being outcomes; expanding the EITC for childless workers and noncustodial parents; updating Unemployment Insurance to reflect the changing nature of work; improving access to affordable housing; increasing Social Security retirement and disability benefits and raising the cap on income subject to taxes; and expanding Medicaid in every state are all strategies that would measurably reduce hardship and increase opportunities among disadvantaged families.

"Mainly, the problem is making too much to receive any kind of assistance but not making enough to make ends meet. It's not about luxury items, going out and having fun. It's just that working a minimum wage job makes rent, phones and everything else really difficult."

—Mother living in the Southwest

Conclusion

Reducing poverty and inequality is fundamentally about building a more inclusive and integrated nation, one in which life chances depend less on circumstances of birth, family, and luck, and one in which people are able to develop their talents fully. All of this can and should benefit the country overall. The striking, though all-too-unfinished, progress of racial and gender economic integration from the mid-20th century onward provides powerful evidence that equalizing opportunity maximizes economic output. Researchers at Stanford Graduate School of Business and the University of Chicago Booth School of Business estimate that reducing employment and education discrimination faced by African Americans and women may be responsible for up to one fifth of total wage growth from 1960 to 2008 (Hsieh, Hurst, Jones, & Klenow, 2013).

As this issue of *Insight* highlights, efforts such as strengthening the EITC represent promising multigenerational strategies for fulfilling the promise of America for tens of millions of children and families. Imagine what we can accomplish as a country when no child or family is hindered by poverty or extreme inequality. With America's economic competitors making impressive investments in children and families (Herman, Post, & O'Halloran, 2013; Cooper, Hersch, & O'Leary, 2012), that vision should become a national imperative. 🌸

References

- Avellar, S., Paulsell, D., Sama-Miller, E., Del Grosso, P., Akers, L., & Kleinman, R. (2014). *Home visiting evidence of effectiveness review: Executive summary*. Office of Planning, Research and Evaluation & Mathematica Policy Research. Retrieved from http://homvee.acf.hhs.gov/HomVEE_Executive_Summary_2014-59.pdf
- Baker, D., & Bernstein, J. (2013). *Getting back to full employment: A better bargain for working people*. Washington, DC: Center for Economic and Policy Research. Retrieved from http://www.cepr.net/documents/Getting-Back-to-Full-Employment_20131118.pdf
- Berg, A. G., & Ostry, J. D. (2011). *Inequality and unsustainable growth: Two sides of the same coin?* Staff Discussion Note, International Monetary Fund. Retrieved from <https://www.imf.org/external/pubs/ft/sdn/2011/sdn1108.pdf>
- Boonstra, H. D. (2008). *The impact of government programs on reproductive health disparities: Three case studies*. *Guttmacher Policy Review*. Retrieved from <https://www.guttmacher.org/pubs/gpr/11/3/gpr110306.html>
- Casey, T. (2014). *Women's poverty in the United States, 2013*. New York, NY: Legal Momentum & The Women's Legal Defense and Education Fund. Retrieved from <http://www.scribd.com/doc/240058539/Legal-Momentum-Poverty-Report-2013>
- Center for Community Change. (2014). *Messaging for economic justice*. Retrieved from <http://www.communitychange.org/wp-content/uploads/2014/07/CCC-Research-Brief.pdf>
- Chetty, R., & Hendren, N. (2015). *Executive summary: The impacts of neighborhoods on intergenerational mobility*. Harvard University. Retrieved from http://www.equality-of-opportunity.org/images/nbhs_exec_summary.pdf
- Children's Defense Fund. (2015). *Ending child poverty now*. Retrieved from <http://www.childrensdefense.org/library/PovertyReport/EndingChildPovertyNow.html>
- Cingano, F. (2014). *Trends in income inequality and its impact on economic growth*. Paris, France: Organisation for Economic Co-operation and Development. Retrieved from http://www.oecd-ilibrary.org/social-issues-migration-health/trends-in-income-inequality-and-its-impact-on-economic-growth_5jxrxjncwv6j-en;jsessionid=1gxzd97aj2wjo.x-oecd-live-02
- Cooper, D., Hersch, A., & O'Leary, A. (2012). *The Competition that Really Matters: Comparing U.S., Chinese, and Indian Investments in the Next-Generation Workforce*. Center for American Progress. Retrieved from <https://www.americanprogress.org/issues/economy/report/2012/08/21/11983/thec-competition-that-really-matters/>
- Dabla-Norris, E., Kochhar, K., Suphaphiphat, N., Ricka, F., & Tsounta, E. (2015). *Causes and consequences of income inequality: A global perspective*. International Monetary Fund. Retrieved from <http://www.imf.org/external/pubs/ft/sdn/2015/sdn1513.pdf>
- Dahl, G. B., & Lochner, L. (2012). *The impact of family income on child achievement: Evidence from the Earned Income Tax Credit*. *American Economic Review*. Retrieved from <http://econweb.ucsd.edu/~gdahl/papers/children-and-EITC.pdf>
- Danziger, S. H. (2007). *Fighting poverty revisited: What did researchers know 40 years ago? What do we know today?* *Focus*. Retrieved from <http://www.irp.wisc.edu/publications/focus/pdfs/foc251a.pdf>
- Defina, R., & Hannon, L. (2013). *The impact of mass incarceration on poverty*. *Crime and Delinquency*. Retrieved from <http://cad.sagepub.com/content/59/4/562.abstract>
- DeNavas-Walt, C., & Proctor, B. D. (2014). *Income and poverty in the United States: 2013*. Current Population Reports. U.S. Census Bureau. Retrieved from <http://www.census.gov/content/dam/Census/library/publications/2014/demo/p60-249.pdf>
- Dutta-Gupta, I. (2011). *Why the upcoming poverty numbers matter*. Center on Budget and Policy Priorities. Retrieved from <http://www.cbpp.org/blog/why-the-upcoming-poverty-numbers-matter>
- Dutta-Gupta, I. (2015). *Why the wealthy always win*. Zocalo Public Square. Retrieved from <http://www.zocalopublicsquare.org/2015/04/22/is-rising-inequality-slowly-poisoning-our-democracy/ideas/up-for-discussion/#Indivar+Dutta-Gupta>
- Dutta-Gupta, I., & Grant, K. (2015). *TANF's not all right*. *The Hill*. Retrieved from <http://thehill.com/opinion/op-ed/240666-tanfs-not-all-right>
- Dynarski, S., Hyman, J., & Whitmore Schanzenbach, D. (2011). *Experimental evidence on the effect of childhood investments on postsecondary attainment and degree completion*. National Bureau of Economic Research. Retrieved from http://users.nber.org/~dynarski/Dynarski_Hyman_Schanzenbach.pdf
- Edelman, P. (2014). *We have blown a huge hole in the safety net*. TalkPoverty.org. Retrieved from <http://talkpoverty.org/2014/05/22/edelman/>
- Emmons, W. R., & Noeth, B. J. (2015). *Why didn't higher education protect Hispanic and Black wealth?* Federal Reserve Bank of St. Louis. Retrieved from <https://www.stlouisfed.org/publications/in-the-balance/issue12-2015/why-didnt-higher-education-protect-hispanic-and-black-wealth>
- Fitz, N. (2015). *Economic inequality: It's far worse than you think*. *Scientific American*. Retrieved from <http://www.scientificamerican.com/article/economic-inequality-it-s-far-worse-than-you-think/>
- Freeman, R., Han, E., Madland, D., & Duke, B.V. (2015). *Bargaining for the American Dream: What Unions do for Mobility*. Center for American Progress. Retrieved from <https://cdn.americanprogress.org/wp-content/uploads/2015/09/08130545/UnionsMobility-report-9.9.pdf>
- Gallagher Robbins, K., & Morrison, A. (2014). *National snapshot: Poverty among women & families, 2013*. National Women's Law Center. Retrieved from <http://www.nwlc.org/sites/default/files/pdfs/povertynapshot2013.pdf>
- Gilens, M. (2014). *Affluence and influence: Economic inequality and political power in America*. Princeton, NJ: Princeton University Press. Retrieved from <http://press.princeton.edu/chapters/i9836.pdf>
- Gimpelson, V., & Treisman, D. (2015). *Misperceiving inequality*. Cambridge, MA: National Bureau of Economic Research. Retrieved from <https://www.nber.org/papers/w21174.pdf>
- Gould, E., Davis, A., & Kimball, W. (2015). *Broad-based wage growth Is a key tool in the fight against poverty*. Economic Policy Institute. Retrieved from <http://www.epi.org/publication/broad-based-wage-growth-is-a-key-tool-in-the-fight-against-poverty/>
- Hartmann, H., Hayes, J., & Clark, J. (2014). *How equal pay for working women would reduce poverty and grow the American economy*. Institute for Women's Policy Research. Retrieved from <http://www.iwpr.org/publications/pubs/how-equal-pay-for-working-women-would-reduce-poverty-and-grow-the-american-economy>

- Herman, J., Post, S., & O'Halloran, S. (2013). The United States is far behind other countries on pre-K. Center for American Progress. Retrieved from <https://www.americanprogress.org/issues/education/report/2013/05/02/62054/th-e-united-states-is-far-behind-other-countries-on-pre-k/>
- Holzer, H. J. (2010). *Penny wise, pound foolish: Why tackling child poverty during the Great Recession makes economic sense*. Center for American Progress & Half in Ten. Retrieved from https://cdn.americanprogress.org/wp-content/uploads/issues/2010/09/pdf/hit_childpoverty.pdf
- Hoynes, H. W., & Patel, A. J. (2015). *Effective policy for reducing inequality? The Earned Income Tax Credit and the distribution of income*. National Bureau of Economic Research. Retrieved from <http://www.nber.org/papers/w21340>
- Hsieh, C., Hurst, E., Jones, C. I., & Klenow, P. J. (2013). *The allocation of talent and U.S. economic growth*. National Bureau of Economic Research. Retrieved from <http://klenow.com/HHJK.pdf>
- Jackson, C. K., Johnson, R., Persico, C. (2014). *The effect of school finance reforms on the distribution of spending, academic achievement, and adult outcomes* (NBER Working Paper Series). Retrieved from <https://www.nber.org/papers/w20118>
- Kautz, T., Heckman, J. J., Diris, R., ter Weel, B., & Borghans L. (2014) *Fostering and measuring skills: Improving cognitive and non-cognitive skills to promote lifetime success*. Organisation for Economic Co-operation and Development. Retrieved from <https://www.oecd.org/edu/cei/Fostering-and-Measuring-Skills-Improving-Cognitive-and-Non-Cognitive-Skills-to-Promote-Lifetime-Success.pdf>
- Kuziemko, I., Norton, M. I., Saez, I., & Stantcheva, S. (2015). How elastic are preferences for redistribution? Evidence from randomized survey experiments. *American Economic Review*, 105(4), 1478–1508. Retrieved from <https://www.aeaweb.org/articles.php?doi=10.1257/aer.20130360>
- Marr, C., Huang, C. C., Sherman, A., & DeBot, B. (2015). *EITC and Child Tax Credit promote work, reduce poverty, and support children's development, research finds*. Center on Budget and Policy Priorities. Retrieved from <http://www.cbpp.org/research/eitc-and-child-tax-credit-promote-work-reduce-poverty-and-support-childrens-development?fa=view&cid=3793>
- Mather, M., & Jarosz, B. (2014). *Persistent racial/ethnic gaps in the U.S.* Population Reference Bureau. Retrieved from <http://www.prb.org/Publications/Reports/2014/us-inequality-racial-ethnic-gaps.aspx>
- National Partnership for Women & Families. (2015). *The Family and Medical Insurance Leave Act (The FAMILY ACT)*. Retrieved from <http://www.nationalpartnership.org/research-library/work-family/paid-leave/family-act-fact-sheet.pdf>
- Reynolds, A. J. (2015). *Cost-effectiveness of early childhood development programs*. Policy Institute for Family Impact Seminars. Retrieved from https://www.purdue.edu/hhs/hdfs/fii/wp-content/uploads/2015/07/s_nmfis03c01.pdf
- Saez, E., & Pikkety, T. (2015). Retrieved from <http://eml.berkeley.edu/~saez/TabFig2013prel.xls>
- Saez, E., & Zucman, G. (2014). *Wealth inequality in the United States since 1913: Evidence from capitalized income tax data* (Working paper). Cambridge, MA: National Bureau of Economic Research. Retrieved from <http://gabriel-zucman.eu/files/SaezZucman2014.pdf>
- Saez, E., & Zucman, G. (2015). *Striking it Richer: The Evolution of Top Incomes in the United States* (Updated with 2014 preliminary estimates). UC Berkeley. Retrieved from <http://eml.berkeley.edu/~saez/saez-USstopincomes-2013.pdf>
- Sherman, A., Trisi, D., & Parrott, S. (2013). *Various supports for low-income families reduce poverty and have long-term positive effects on families and children*. Center on Budget and Policy Priorities. Retrieved from <http://www.cbpp.org/research/various-supports-for-low-income-families-reduce-poverty-and-have-long-term-positive-effects>
- Short, K. (2014). *The supplemental poverty measure: 2013*. U.S. Census Bureau. Retrieved from <https://www.census.gov/content/dam/Census/library/publications/2014/demo/p60-251.pdf>
- Smith, A. (1904). *An inquiry into the nature and causes of the wealth of nations*. Retrieved from <http://www.econlib.org/cgi-bin/searchbooks.pl?searchtype=BookSearchPara&cid=smWN&query=%22The+Greeks+and+romans+lived%2C+i+suppose%22>
- The Stanford Center on Poverty & Inequality. (2014). *State of the union: The poverty and inequality report, 2014*. Retrieved from https://web.stanford.edu/group/scspi/sotu/SOTU_2014_CPI.pdf
- Stiglitz, J. E. (2015). *Rewriting the rules of the American economy: An agenda for growth and shared prosperity*. Roosevelt Institute. Retrieved from <https://static1.squarespace.com/static/5547c707e4b0e8aadbc53a05/t/55520236e4b0872f41a7058a/1431438002852/Rewriting+the+Rules+Report+Full+Report+-+Single+Page+Final.pdf>
- Urban Institute. (2015). *Nine charts about wealth inequality in America*. Retrieved from <http://datatools.urban.org/Features/wealth-inequality-charts/>
- U.S. Census Bureau. (2014). *Income and poverty in the United States: 2013*. Retrieved from <http://www.census.gov/hhes/www/poverty/data/incpovhlth/2013/index.html>

Overview of the Earned Income Tax Credit

By Robert Greenstein, Center on Budget and Policy Priorities

Introduction

The federal Earned Income Tax Credit (EITC), which goes to low- and moderate-income working people, isn't as well-known as other major parts of the nation's safety net. But it's one of our most effective antipoverty programs. Along with the low-income component of the Child Tax Credit (CTC), the EITC encourages work, helps offset the cost of raising children, and lifts millions of Americans out of poverty. Moreover, important new research suggests that these credits also reduce poverty over the next generation.

The EITC is a proven success in "making work pay" and reducing poverty. It has enjoyed bipartisan support, and successive presidents and congresses of both parties have left their imprints on it. President Ford signed it into law in 1975; Presidents Carter, Reagan, the first Bush, Clinton, and Obama proposed EITC increases; and every president from Carter to Obama signed an increase into law.

Nearly 28 million working families and individuals received the EITC in 2013 (the latest year for which we have data). Nearly 5 million workers outside of metropolitan areas, with almost 6 million children, claimed the EITC in 2013. Roughly 14 million White Americans, 5 million African Americans, 9 million Hispanic Americans, and 1 million Asian Americans receive the EITC each year; the credit is especially important for people of color since they comprise a disproportionate share of the low-wage workforce.¹

By itself, the EITC lifted about 6.2 million people, including 3.2 million children, out of poverty in 2013 and reduced the severity of poverty for another 21.6 million people, including 7.8 million children. Together, the EITC and CTC lift 9 million people out of poverty and make 22 million others less poor. The EITC and CTC also lift 5 million children out of poverty, more than any other federal program. (These figures use the Supplemental Poverty Measure, which, unlike the official poverty measure, counts tax credits and non-cash benefits as income.)

Beyond its short-term benefits, the EITC generates benefits at virtually every stage of life, an impressive body of recent research indicates. Starting from infancy — when higher tax credits have been linked with more prenatal care, less maternal stress, and better infant health — children who benefit from expanded tax credits do better throughout childhood and have higher odds of finishing high school and going to college. The EITC also has been linked to significant increases in college enrollment by making college more affordable for families with

high-school seniors. The education and skill gains associated with working-family tax credits likely keep paying off through higher earnings and employment for many years, researchers say. In fact, the EITC "may ultimately be judged one of the most successful labor market innovations in U.S. history," says the University of California's Hilary Hoynes², due to its ability to encourage work in the near term and promote a stronger workforce over the longer term, and also to reduce poverty markedly.

Unfortunately, key EITC and CTC provisions that allow more working-poor families to receive the CTC, provide a larger EITC to families with more than two children, and reduce the EITC's "marriage penalty" (the reduction in EITC for some couples who file jointly as a married couple, as compared to the EITCs they would get if they weren't married and filed separately) are scheduled to expire at the end of 2017. This will cause millions of low-income working families to lose all or part of their credits and push many into poverty. Policymakers should make these provisions permanent. Without them, more than 16 million people, including almost eight million children, will be pushed into or deeper into poverty.

How the EITC Works

To claim the EITC, a taxpayer must have earnings from employment. Workers claim the credit when they file their federal income tax return, and most recipients claim the credit for relatively short periods (such as a year or two) at a time (Dowd & Horowitz, 2011).

Working families with children and with incomes up to about \$52,000 may be eligible for the EITC, depending on their marital status and number of dependent children. The average EITC was roughly \$2,970 for a family with children during the 2012 tax year. But the EITC is meager for working people who aren't raising children in the household. The average EITC for workers without children who received a credit was just about \$270 in 2012, and those under age 25 are ineligible.

The EITC's size depends on a recipient's income, marital status, and number of children. For families with very low

¹ Center on Budget and Policy Priorities analysis of IRS 2013 data and U.S. Census Bureau's March 2014 Current Population Survey public use file.

² Hilary Hoynes, "A Revolution in Poverty Policy: The Earned Income Tax Credit and the Well-Being of American Families," *Pathways*, Summer 2014, pp. 23-27, http://web.stanford.edu/group/scspi/_media/pdf/pathways/summer_2014/Pathways_Summer_2014.pdf.

earnings that are just gaining a toehold in the labor market, the credit rises as family earnings rise, offsetting the phase-down of some other public benefits as earnings increase. The EITC thus boosts families' overall income and strengthens incentives to work. It gradually phases out at higher income levels.

The EITC is “refundable”; this means that if it exceeds a low-wage worker’s income tax liability, the Internal Revenue Service (IRS) refunds the balance to the worker. Eligible workers who earned too little to owe income tax can thus still receive a refund from IRS, in the amount of their EITC. Families mostly use their EITC benefits to pay for necessities, repair homes, maintain their cars to commute to work, and, in some cases, get more education or training.³

“The biggest challenges right now with being low income is just budgeting. Not having enough for everything your family needs. Unexpected expenses. Having to say no to my kids often.”

—Mother from the East



State EITCs

Twenty-six states plus the District of Columbia have created their own EITCs to supplement the federal credit and further bolster the wages of struggling families. Typically, the state credit is set at a fixed percentage of the federal credit and uses the same eligibility rules. All but three states with EITCs allow working households to keep the full value of their credit, even if it exceeds their state income tax liability.

More than one in three recipients of the federal EITC can now qualify for a state EITC. State EITCs boost the earnings of working families by about \$4 billion a year. In addition, two localities —Montgomery County (MD) and New York City — offer a supplemental local credit.

Since 2011, California, Connecticut, Colorado, and Ohio have created EITCs, and various other states have strengthened their existing credits. This year alone, California became the 26th state with an EITC, and four other states expanded their credits (MA, ME, NJ, RI). On the other hand, policymakers in a few states have sought (in a few cases successfully) to scale back or eliminate their EITCs in recent years. North Carolina, for example, allowed its credit to end after tax year 2013 to help make room in its budget for tax cuts primarily benefiting wealthy households and corporations. This year attempts were made to cut back the Kansas credit to fill a shortfall caused by massive tax cuts, and lawmakers in Michigan — after cutting the state EITC substantially in 2011 — have considered eliminating it to help pay for road repair.

Encouraging Work

The EITC is designed to encourage and reward work because, as noted, it grows with every dollar of earnings until reaching its maximum value. This creates incentives for people to leave welfare for work and for low-wage workers to work more.

This incentive feature has been very successful. “The overwhelming finding of the empirical literature is that the EITC has been especially successful at encouraging the employment of single parents, especially mothers,” write Georgetown University’s Nada Eissa and Hoynes (Eissa & Hoynes, 2006). While some policymakers point to the 1996 welfare law and its creation of Temporary Assistance for Needy Families (TANF) as the main reason for more work among single mothers, the research indicates that the EITC expansions of the 1990s were as big — or bigger — a factor.⁴

³ See, for example: Mendenhall, R., Edin, K., Crowley, S., Sykes, J., Tach, L., Kriz, K., & Kling, J. R. (2010). *The role of Earned Income Tax Credit in the budgets of low-income families*, National Poverty Center., Retrieved from http://npc.umich.edu/publications/u/working_paper10-05.pdf

⁴ Center on Budget and Policy Priorities analysis of results from Grogger, J. (2003). The effects of time limits, the EITC, and other policy changes on welfare use, work, and income among female-head families, *Review of Economics and Statistics*.

By boosting employment among single mothers, the EITC also shrinks cash welfare caseloads. The 1990 and 1993 expansions induced more than a half-million families to move from cash welfare to work, research found.

Moreover, by boosting the employment and earnings of working-age women, the EITC also boosts their Social Security retirement benefits, which are based on a person's work history. Higher Social Security benefits, in turn, reduce the extent and severity of poverty in old age.

Some express concern that the EITC's benefit phase-down above certain income levels creates a disincentive to work. But there's little evidence of it, except modestly among second earners in a family (and that may have the positive effect of allowing parents in two-earner families to devote more time to raising their young children). All told, the EITC's overwhelming employment effect is to induce many more people to work.

Improving Infant and Maternal Health

The EITC may improve the health of infants and mothers, research finds. The most notable evidence comes from a study comparing mothers who were in the demographic and income groups targeted for the largest EITC increases in the 1990s with mothers who were likely eligible for the smallest increases (Hoyne, Miller, & Simon, 2012). Infants of mothers who likely received the largest EITC increases had greater improvements in low birthweight, premature birth, and other birth indicators.

In addition, studies show that mothers receiving the largest EITC increases were likelier to receive prenatal care, including care before the critical third trimester. They also reported lower stress levels, and were less likely to smoke and drink during pregnancy.⁵

Improving Children's School Performance

Gordon Berlin, the president of MDRC, one of the nation's premier evaluation and research organizations, explains:

[There is] a remarkably strong body of research — much of it based on large-scale, well-implemented, experimental research designs — showing that supplementing the earnings of parents helps raise families out of poverty and improves the school performance of young children. . . . We have reliable evidence involving thousands of families in multiple studies demonstrating that “making work pay” [through cash supplements to low earners] causes improvements in young children's school performance.⁶

In particular, income support from the EITC has been linked to better academic achievement for elementary and middle-school students. When low-income families receive larger federal or state EITCs, their children tend to score better on tests of reading and (particularly) math, compared with children from largely similar families that aren't eligible for large EITC expansions. They're also likelier to finish high school (Maxfield, 2013).

Children in families that receive larger EITCs also are likelier to go to college, the evidence shows, both because they do better in school and because larger tax refunds make college more affordable for low-income families with high-school seniors (Manoli & Turner, 2014).

Boosting Future Earnings

The EITC's pro-work benefits extend to the next generation. Because children in families receiving working-family tax credits tend to do better and go further in school, they likely earn more as adults. In fact, each \$1 in tax credits may boost a child's cumulative future earnings by more than \$1, researchers project (Chetty, Friedman, & Rockoff, 2011).

For young children in low-income families, even relatively modest increases in family income — regardless of the source — are associated with more work and higher earnings in adulthood. One study found that for each additional \$3,000 in annual family income that children in poor families received before age 6, they worked an additional 135 hours a year between ages 25 and 37 (the years that the study examined) and their annual earnings rose by an average of 17% (Duncan, Ziol-Guest, & Kalil, 2010).

One reason why poorer children may have lower work effort and earnings in adulthood than middle- and upper-income children, according to an emerging body of research, is that as children they are likelier to experience poor health and intensive stress that can affect brain and other development and have effects extending into adulthood (Ziol-Guest, Duncan, Kalil, & Boyce, 2012).

Continuing Key Provisions, Helping Childless Workers

Several critical provisions of the EITC and the low-income component of the CTC are slated to expire at the end of 2017. Millions of low-income working families will lose all or part of their EITC and CTC if policymakers don't extend these provisions:

- The minimum earnings needed to qualify for *any* CTC would jump from \$3,000 to \$14,700, and the earnings needed to qualify for the *full* CTC would jump from \$16,330 to more

⁵ See: Evans, W. N., & Garthwaite, C. L. (2014). Giving Mom a break: The impact of higher EITC payments on maternal health. *American Economic Journal: Economic Policy*, 6(2), 258–290; Baker, K. (2008). *Do cash transfer programs improve infant health: Evidence from the 1993 expansion of the Earned Income Tax Credit* (University of Notre Dame mimeo). Retrieved from http://economics.nd.edu/assets/24011/baker_paper.pdf; and Strully, K. W., Rehkopf, D. H., & Xuan, Z. (2010, August). Effects of prenatal poverty on infant health: State Earned Income Tax Credits and birth weight. *American Sociological Review*, 1–29. Retrieved from <http://www.irp.wisc.edu/newsevents/workshops/2011/participants/papers/15-Strully.pdf>

⁶ Remarks by Gordon L. Berlin, President, MDRC, at the National Summit on America's Children, May 22, 2007. Retrieved from <http://www.mdrc.org/publication/investing-parents-invest-children>



than \$28,000 for a family with two children. In addition, a single mother with two children who works full time at the minimum wage (thus earning \$14,500) would lose her entire CTC of \$1,725 in 2018.

- Many married couples would face EITC cuts and, as a result, larger marriage penalties. To reduce marriage penalties, the EITC currently begins to phase out at an income level that's \$5,000 higher for married couples than single filers. After 2017, it would be just \$3,000 higher, shrinking the EITC for many low-income married filers and increasing the marriage penalty for a substantial number of two-earner families.
- Large families, as well, would face an EITC cut. After 2017, the maximum EITC for families with more than two children would fall by over \$700 (to the same EITC level as that for families with two children).

While making the EITC and CTC provisions permanent, policymakers should also plug a glaring hole in the tiny EITC for childless adults and noncustodial parents who are not raising minor children in their homes. Such workers are the sole group that the federal tax system taxes into or deeper into poverty (Marr & Huang, 2015).

President Obama, House Ways and Means Committee Chairman Paul Ryan, and numerous lawmakers have proposed making the EITC more adequate for this largely left-out group. Making more childless workers eligible for the EITC, including those working full time at the minimum wage, and expanding the very small credit for childless workers hold strong promise of boosting employment and reducing poverty.

Conclusion

For four decades, the EITC has earned bipartisan praise as a pro-work success story that helps low-income working families make ends meet and stay out of poverty. New research suggests it does even more, leading to improvements in infants' and mothers' health, children's school performance, and children's future earnings. These findings suggest that the EITC fights poverty not only in this generation but also in the next one by helping children reach their full potential. ✨

References

- Chetty, R., Friedman, J. N., & Rockoff, J. (2011, November). *New evidence on the long-term impacts of tax credits* (Statistics of Income Paper Series). Retrieved from <http://www.irs.gov/pub/irs-soi/11rpchettyfriedmanrockoff.pdf>
- Dowd, T., & Horowitz, J. B. (2011, April 11). Income mobility and the Earned Income Tax Credit: Short-term safety net or long-term income support. *Public Finance Review*.
- Duncan, G. J., Ziol-Guest, K. M., & Kalil, A. (2010, January/February). Early-childhood poverty and adult attainment, behavior, and health. *Child Development*, 81(1), 306–325.
- Hoynes, H. W., Miller, D. L., & Simon, D. (2012, July). *Income, the Earned Income Tax Credit, and infant health* (NBER Working Paper No. 18206). Retrieved from <http://www.nber.org/papers/w18206>
- Manoli, D. S., & Turner, N. (2014, January). Cash-on-hand and college enrollment: Evidence from population tax data and policy nonlinearities (NBER Working Paper No. 19836). Retrieved from <http://www.nber.org/papers/w19836>
- Marr, C., & Huang, C.-C. (2015). Strengthening the EITC for childless workers would promote work and reduce poverty. Center on Budget and Policy Priorities. Retrieved from <http://www.cbpp.org/research/strengthening-the-eitc-for-childless-workers-would-promote-work-and-reduce-poverty>
- Maxfield, M. (2013, November 14). *The effects of the Earned Income Tax Credit on child achievement and long-term educational attainment* (Michigan State University Job Market Paper). Retrieved from <https://www.msu.edu/~maxfiel7/20131114%20Maxfield%20EITC%20Child%20Education.pdf>
- Nissa, N., & Hoynes, H. (2006, September). Behavioral Responses to Taxes: Lessons from the EITC and Labor Supply. (NBER). <http://www.nber.org/chapters/c0063.pdf>
- Ziol-Guest, K. M., Duncan, G. J., Kalil, A., & Boyce, W. T. (2012, October 16). Early childhood poverty, immune-mediated disease processes, and adult productivity, *Proceedings of the National Academy of Sciences of the United States of America*, 109(suppl 2), 17289–17293.

Using the Earned Income Tax Credit to Encourage Work and Increase Income from Work

By David Neumark, University of California, Irvine, National Bureau of Economic Research and Institute for the Study of Labor

Introduction

The Earned Income Tax Credit (EITC) supplements earnings for low-income families and has grown into the major U.S. program (around \$60 billion annually) to boost earnings of working people. In addition, many states supplement the federal EITC.

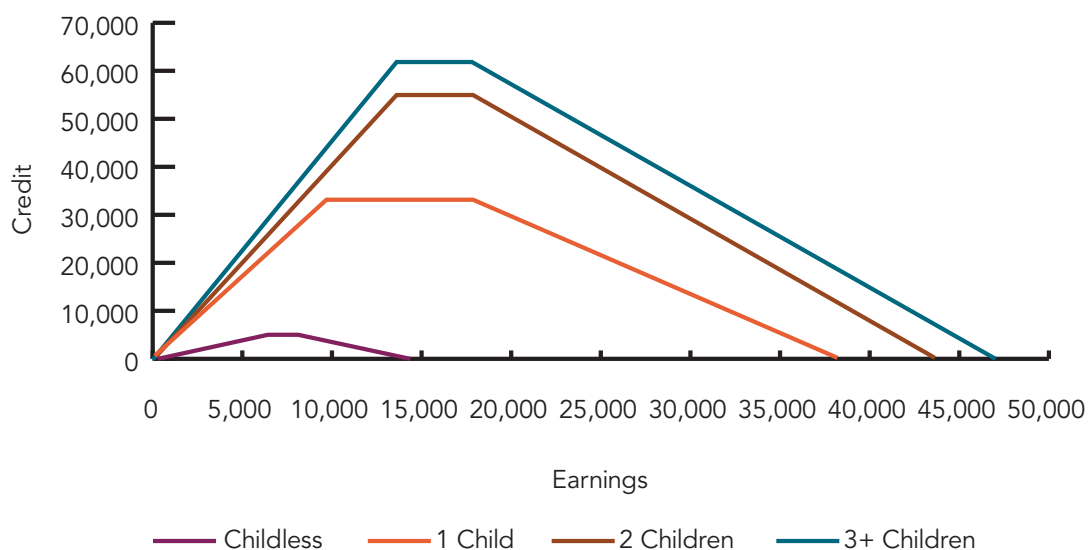
Figure 1 shows key features of the federal EITC. First, it provides supplemental income only to those who are working. Second, it provides a growing subsidy on the upward-sloping part of the schedule (the “phase-in” range), and then at higher income a higher implicit tax rate as the subsidy is phased out. Third, the subsidy value varies sharply with the number of eligible children in a family (i.e., living with the taxpayer). The subsidy and maximum payment is trivial for those without children, but both are much higher for those with children. For example, for a family with two children, in 2014, the maximum credit that could be earned was \$5,460; over the first \$13,650 in earnings, this represents a 40% subsidy to earnings. Finally, note that the EITC is based on family income, and in particular low

family income, and hence will tend to go to single-parent families, in which incomes are much lower on average.

These features of the EITC suggest that the EITC will have two principal effects — encouraging work among low-income eligible adults and increasing incomes of low-income families. This essay reviews the evidence on these effects and considers issues pertaining to expanding the EITC, as well as some of its potential shortcomings and how they might be addressed.

There is overwhelming evidence that a higher EITC does, in fact, increase employment of the group whose employment is most likely to be affected because of both low incomes and higher costs of employment— specifically, single mothers.

Figure 1: Earned Income Tax Credit by Income and Number of Children



Note: The number of children refers to the number of *eligible* children in the tax unit.

Source: <http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?DocID=36&Topic2id=40&Topic3id=42> (viewed October 23, 2014).

Evidence

There is overwhelming evidence that a higher EITC does, in fact, increase employment of the group whose employment is most likely to be affected because of both low incomes and higher costs of employment — specifically, single mothers (Hotz & Scholz, 2003; Hoffman & Seidman, 2003). There is also the potential for labor supply reductions among those already working, in particular secondary workers in families; some evidence points in this direction, but it is ambiguous (Eissa & Hoynes, 2011). Overall, existing studies find that the EITC increased labor supply among women (e.g., Dickert, Houser, & Scholz, 1995; Meyer & Rosenbaum, 2001). We also know that the EITC targets low-income families well. Liebman (1998) and Scholz (1994) showed that a large proportion of EITC payments went to families living below the federal poverty line.

In more recent work, Neumark and Wascher (2011) estimated the effects of the multitude of state expansions in the EITC in the 2000s; in the period they studied, from 1996 to 2007, the number of states with an EITC that supplemented the federal EITC increased from seven states to 19 states and the District of

Columbia.¹ The state-level expansions can be used to provide more rigorous evidence of the effects of the EITC, because they provide policy variation independent of national-level changes that may differentially influence families with different numbers of children.

Neumark and Wascher focused on family earnings of families with heads between the ages of 21 and 44, an age range when families are most likely to have children and be eligible for the EITC. It uses two metrics: the change in the probability that a family's earnings are below the poverty line and the change in the probability that family earnings are below half of the poverty line ("extreme poverty"). The focus on earnings provides a strict test of the power of the EITC to increase income from work through changing work incentives, by excluding the work-contingent transfers of the EITC (which are also excluded from official U.S. poverty calculations), as well as other transfers that can be affected by earnings.

¹ State EITCs were implemented in additional states subsequently.

Table 1:

Estimated Effects of EITC on Family Earnings Relative to Poverty, Family Heads, or Individuals, Aged 21–44, 1997–2006

	Family head or individual	Single female family head or individual	Single female family head or individual, high-school degree at most	Single female family head or individual, Black or Hispanic
P(Earnings < Poverty)	(1)	(2)	(3)	(4)
EITC × kids	-.04 (.07)	-.16 (.17)	-.24 (.18)	.06 (.28)
EITC	-.00 (.05)	-.06 (.08)	-.02 (.10)	-.12 (.18)
P(Earnings < .5 Poverty)				
EITC × kids	-.09 (.06)	-.34* (.18)	-.42* (.23)	-.14 (.25)
EITC	.02 (.04)	.00 (.06)	.05 (.09)	-.14 (.14)
N	362,811	98,327	65,839	34,267

Notes: Based on CPS Annual Demographic Files. All estimates are weighted, and standard errors are clustered on states. Linear probability estimates are reported. ***, **, and * indicate that the estimate is significantly different from zero at the 1%, 5%, and 10% level respectively. The regression also includes controls for the number of children, dummy variables for education (high-school dropout, high-school degree, some college, bachelor's degree or higher), dummy variables for number of children as well as the number of children under age 6 (all observed values), dummy variables for marital status (never married, married spouse present, married spouse absent, and divorced, widowed, or separated), dummy variables for Black or Hispanic, age and its square, the state unemployment rate, and state and year fixed effects. In addition, the model includes a full set of interactions between Kids and both the year dummy variables and the state dummy variables. The estimated coefficients of the EITC–kids interactions are robust to including state-specific linear trends, or state–year interactions; in the latter specifications the main EITC effect drops out. The sample is restricted to heads of families, primary individuals, or unrelated individuals. The estimated coefficients of the EITC–kids interactions are robust to including state-specific linear trends, or state–year interactions.

Source: Neumark and Wascher (2011).

The results are reported in Table 1. The generosity of the EITC is measured by the percentage state supplement to the federal EITC; the latter was unchanged over this period. The coefficient of the interaction between the EITC and an indicator for number of dependent children age 18 or under in the home (which is what is measured in the Current Population Survey [CPS]) captures the effect of the EITC, because the EITC is much more generous for families with children. In technical terms, the effects of the EITC \times number of kids interaction is a difference-in-difference-in-differences estimator that estimates the effect of the EITC from the *differential* effect for those with and without children; the latter provide a control for shocks at the state-by-year level that affect both those eligible and not eligible for the EITC.

A more generous EITC is associated with reductions in the proportion of affected families with very low earnings, and the estimates are larger for families headed by single females or less-educated single females. For the poverty-line regressions, none of these estimates is statistically significant. However, two are statistically significant for the probability that family earnings are below half of the poverty line. Overall, the evidence indicates that the EITC is effective at boosting the earnings of very poor families — and recall that this is a strong test because it does not factor in the actual EITC payment.

“The EITC didn't help to get me a promotion but it helped me to maintain my current position because I got a more reliable vehicle to drive to work every day.”

— Mother from the East coast

Earlier evidence (Neumark & Wascher, 2001) points to similar conclusions. The latter suggests that increases in state EITC generosity raise the probability that family earnings rise above the poverty level, and also raise the earnings, on average, of families with children that are initially below the poverty line. In contrast, there is no effect of pushing near-poor families into poverty (based on earnings), stemming from adverse effects on hours or on earnings of those initially near-poor. The estimates imply that the average increase in the federal credit rate over the sample period (4 percentage points) reduced the poverty rate by nearly 3 percentage points via its effect on earnings.

Expanding the EITC for Childless Adults

President Obama recently proposed increasing the maximum credit to \$1,000, as well as increasing the income level at which the credit is fully phased out so that more low-income childless people will benefit from the higher credit.² An expansion of the EITC for childless adults would create additional incentives for employment of eligible individuals, as well as boost income for those employed. The higher income level at which the credit is fully phased out has only the latter effect.

The core argument for expanding the EITC for individuals without eligible children is to offset the declining returns to

work for low-skilled men stemming in large part from declining real wages at the bottom of the wage distribution (part of the long-run increase in wage inequality). Multiple benefits of a more generous EITC — acting via both increased earnings and higher employment — are conjectured (Berlin, 2007). A higher EITC, by increasing the incentive to work, could have long-term positive effects on earnings via increases in labor market experience. It could also, by boosting incomes, make less-skilled individuals more economically attractive as marriage partners, and hence increase marriage rates and decrease out-of-wedlock childbearing. In addition, Carrasso, Holzer, Maag, and Steuerle (2008) point out that many noncustodial fathers face very high marginal tax rates because of collection of child-support payments, which a subsidy from an expanded EITC could help offset.

Evidence for men comes from the New Hope program, an experiment run in Milwaukee in the late 1990s that offered work-contingent supplements — including to single men. The results suggest that supplements to earnings for single men produced positive effects on employment, earnings, and family income, even up to five years after the program, although many of the estimated effects were not statistically significant (Duncan, Hill, & Tetenov, 2007). Recent work by Autor, Dorn, and Hansen (2014) suggests that exogenous labor demand shocks (from local labor market exposure to increases in competition from Chinese manufacturing) that reduce male employment opportunities lead to lower marriage rates, more teen births, and more children living in single-parent or poor households. There appears to be, as yet, no evidence on how an expanded EITC for individuals might translate into more resources for children of non-custodial parents. Clearly, as Scholz (1994) points out, if such a policy would lead to major social gains beyond increased income, such as reductions in crime and fewer teen births, then the benefits could far outweigh the costs.

However, we have to be aware of potential tradeoffs, because when the EITC strengthens employment incentives for one group, it increases competition with other groups, which can lower the latter group's earnings. Neumark and Wascher (2011) showed that the currently structured EITC, which boosts employment of single mothers, has negative spillover effects on other less-skilled individuals who are “ineligible” for the EITC, but who may compete for the same jobs. Specifically, Neumark and Wascher looked at less-educated childless men and women between the ages of 21 and 34, and subgroups among these, such as less-skilled minorities and less-skilled minority single men.

As Table 2 shows, for less-educated, childless individuals, the estimated EITC effects on wages, employment, and earnings are negative, although not statistically significant. However, for less-educated Blacks and Hispanics, the estimated effects of the EITC on employment and earnings are negative and statistically significant, and the point estimates are larger. The results for less-educated single minority men are stronger still, with the

² See http://www.whitehouse.gov/sites/default/files/docs/eitc_report.pdf, viewed May 16, 2014.



Table 2:

Estimated Effects of EITC on Low-Skilled, Childless Individuals, Aged 21–34, 1997–2006

Low-skilled treatment group	Less-educated individuals	Less-educated Black or Hispanic	Less-educated single Black or Hispanic men
Log wages	(1)	(2)	(3)
EITC × low-skill	-.10 (.09)	-.11 (.08)	-.13 (.09)
EITC	.08 (.07)	.06 (.10)	.08 (.11)
N	131,181	79,362	67,399
Employment			
EITC × low-skill	-.05 (.05)	-.12** (.05)	-.16*** (.05)
EITC	.02 (.04)	.03 (.03)	.01 (.03)
N	150,486	90,408	74,913
Log earnings			
EITC × low-skill	-.58 (.49)	-1.32*** (.44)	-1.75*** (.56)
EITC	.35 (.38)	.40 (.37)	.35 (.29)
N	150,486	90,408	74,913

Notes: Most notes from Table 1 apply, except those pertaining to variables measuring the number of children. The log wage regressions condition on positive earnings and hours of work in the previous year. “Less-educated” means that the individual has a high-school degree at most. The low-skilled treatment group is defined in the column heading. The control group does not change across columns, and always includes all those with at least some college (regardless of race, ethnicity, or marital status). The estimated coefficients of the EITC–low-skill, MW–low-skill, and EITC–MW–low-skill interactions are robust to including state-specific linear trends, or state–year interactions.

Source: Neumark and Wascher (2011).

estimates pointing to negative effects of the EITC on wages, employment, and earnings.

Table 3 presents additional evidence of these negative spillovers, focusing on how many women are eligible for the EITC, measured alternatively as the percentage of tax returns in each state that claimed the federal EITC or share of single mothers in the state. Neither measure directly corresponds to the share of EITC-eligible women, but both should be highly correlated with it. The results indicate that the spillover effects of the EITC on low-skilled, childless individuals are larger in states where a greater proportion of women are potentially affected by the EITC. In the wage regression estimates in column (1), for example, the negative estimated coefficient of the interaction between the EITC variable, the low-skill indicator, and the share of EITC filers implies that the negative effect of the EITC on the wages of childless, low-skilled men and women is stronger in states where a higher percentage of tax filers claimed the EITC.

This evidence indicates that the EITC adversely affects those who compete with the less-skilled women with children whose employment increases because of the EITC. Turning this around, the implication is that expanding the EITC among

those *without* children to bring more of them into the labor market is likely to shift some of the benefits of the EITC program as a whole away from families, as the eligible participants with children face increased labor supply from unrelated individuals, while at the same time encouraging employment and increasing earnings and income among less-skilled men who are not in families. This may be an acceptable tradeoff, in light of some of the arguments above, but this tradeoff should not be ignored.

There are a number of unknowns regarding these tradeoffs. First, would there be substantial increases in resource flows to the children of noncustodial parents? Second, could an expanded EITC lead, in the longer run, to substantial earnings gains for less-skilled men, and, via effects on marriage and childbearing, eventually reduce reliance on the EITC? Third, would the proposed expansion of the EITC largely affect individuals already working, making it more likely to reduce their labor supply without changing their income much?³

³ Mulheirn and Pisani (n.d.) report a positive employment effect from the introduction of an earned income tax credit for childless adults in the United Kingdom.

Table 3: Estimated EITC Effects on Low-Skilled (Less-Educated), Childless Individuals, Aged 21–34, Variation with Share Affected by EITC, 1998–2006

	Using share filing for EITC	Using share of single mothers
	(1)	(2)
Log wages		
EITC × low-skill	-.22*** (.05)	-.05 (.04)
EITC	.09 (.08)	.01 (.07)
EITC × low-skill × 1997 filing/single mother share (× 10)	-.38** (.15)	-.84** (.34)
N	120,976	120,976
Employment		
EITC × low-skill	-.14*** (.01)	-.04** (.02)
EITC	-.02 (.05)	-.03 (.04)
EITC × low-skill × 1997 filing/single mother share (× 10)	-.21*** (.06)	-.55*** (.15)
N	139,096	139,096
Log earnings		
EITC × low-skill	-1.54*** (.16)	-.43** (.18)
EITC	-.03 (.53)	-.19 (.48)
EITC × low-skill × 1997 filing/single mother share (× 102)	-.23*** (.07)	-.60*** (.16)
N	139,096	139,096

Notes: The data on filing share are derived from the Internal Revenue Service’s Stakeholder Partnerships, Education, and Communication (IRS-SPEC) database. Data from 1997 are omitted, to avoid endogeneity of the 1997 shares. The mean filing share across states in 1997 is 0.16, ranging from 0.09 in Alaska to 0.32 in Mississippi. The mean share of the adult population that consists of single mothers (with children at home) is 0.07, ranging from 0.05 in Maine to 0.10 in Mississippi.

Source: Neumark and Wascher (2011).

Potential Limitations of the EITC

The EITC has some potential limitations. First, it does nothing for those who cannot work (in contrast to a negative income tax, discussed below). Second, one role of income-support programs is to partially insulate families from adverse effects of the business cycle. Bitler, Hoynes, and Kuka (2014) show that the EITC does this for married couples, for whom reductions in combined incomes move them to lower incomes along the phase-out range of the EITC, or make them eligible, thereby increasing EITC payments. However, for single parents, job loss can end eligibility or lower earnings on the phase-in range, implying smaller payments, so that EITC payments for these families — along with their earnings — decline during recessions.

Finally, the EITC lowers market wages, which leads some critics to deride the EITC “corporate welfare,” with the taxpayers subsidizing the low wages paid by employers.⁴ This argument is ill-founded from the perspective of increasing employment, which comes about precisely because the EITC lowers labor

costs for employers; workers earning the EITC have higher earnings per hour factoring in the credit. Nevertheless, as we have seen, the EITC can lower wages for low-skilled workers who are not eligible for the EITC. Indeed, Rothstein (2011) presents simulations suggesting that employers capture substantial gains via lower wages (see also Leigh, 2010).


Arguing that a higher minimum wage is needed to eliminate the wage reduction from the EITC is overly simplistic if all that it does is to eliminate the wage reduction from the increase in labor supply. However, Neumark and Wascher (2011) suggest that a higher minimum wage can enhance the effects of the EITC. If reservation wages (i.e., the wage needed to draw workers into the labor market) vary across low-skilled workers, then a higher minimum wage *plus* an EITC may lead those with the highest reservation wages to seek work, displacing those with

⁴ See, e.g., <http://www.bloomberg.com/news/2013-11-13/how-mcdonald-s-and-wal-mart-became-welfare-queens.html>, viewed May 19, 2014.



lower reservation wages. If, as seems plausible, single mothers with children have particularly high reservation wages, then combining the EITC with a higher minimum wage may enhance the beneficial distributional effects of the EITC, and Neumark and Wascher find that this combination of policies leads to higher employment and earnings for single women with children. At the same time, this same policy combination has more adverse effects on groups that are not eligible for the EITC — such as teenagers and less-skilled minority men.

A More Generous EITC as a Response to Income Inequality?

Aside from expanding the EITC for those without children, we could make the overall EITC more generous. The EITC is likely the best policy to address rising income inequality. The EITC encourages work — which makes the policy more politically palatable — and through this channel likely has beneficial longer-term effects.⁵ In addition, because it is financed by taxes, the EITC (in contrast to a higher minimum wage) redistributes from those who earn the most; because it targets low-income families well, it redistributes toward those who earn the least.⁶ 

⁵ There is only limited evidence of this; see Dahl et al. (2009).

⁶ See http://www.nytimes.com/2014/01/05/business/help-the-working-poor-but-share-the-burden.html?src=recg&c_r=0, viewed May 19, 2014.

References

Autor, D., Dorn, D., & Hansen, G. (2014). The labor market and the marriage market: How adverse employment shocks affect marriage, fertility, and children's living circumstances. Unpublished paper.

Berlin, G. L. (2007). Rewarding the work of individuals: A counterintuitive approach to reducing poverty and strengthening families. *The Future of Children*, 17, 17–42.

Bitler, M., Hoynes, H., & Kuka, E. (2014). *Do in-work tax credits serve as a safety net?* (NBER Working Paper No. 19785).

Carrasso, A., Holzer, H. J., Maag, E., & Steuerle, C. E. (2008). *The next stage: Encouraging work and family formation among low-income men* (Urban-Brookings Tax Policy Center Discussion Paper No. 28).

Dahl, M., DeLeire, T., & Schwabish, J. (2009). Stepping stone or dead end? The effect of the EITC on earnings growth. *National Tax Journal*, 62, 329–346.

Dickert, S., Houser, S., & Scholz, J. K. (1995). The Earned Income Tax Credit and transfer programs: A study of labor market and program participation. *Tax Policy and the Economy*, 9, 1–50.

Duncan, G. J., Hill, H. D., & Tetenov, A. (2007). The persistence of New Hope's labor market impacts: How long? How real? Unpublished paper.

Eissa, N., & Hoynes, H. (2011). Redistribution and tax expenditures: The Earned Income Tax Credit. *National Tax Journal*, 64, 689–730.

Hotz, V. J., & Scholz, J. K. (2003). The Earned Income Tax Credit. In R. A. Moffitt (Ed.) *Means-tested transfer programs in the United States* (pp. 141–198). New York: Russell Sage Foundation.

Leigh, A. (2010). Who benefits from the Earned Income Tax Credit? Incidence among recipients, coworkers, and firms. *B.E. Journal of Economic Analysis & Policy*, 10, 1 (online).

Liebman, J. B. (1998). The impact of the Earned Income Tax Credit on incentives and the income distribution. In J. Poterba (Ed.) *Tax policy and the economy*, volume 12 (pp. 83–120). Cambridge, MA: MIT Press.

Meyer, B. D., & Rosenbaum, D. T. (2001). Welfare, the Earned Income Tax Credit, and the labor supply of single mothers. *Quarterly Journal of Economics*, 116, 1063–1114.

Moffitt, R. A. (2003). The Negative Income Tax and the evolution of U.S. welfare policy. *Journal of Economic Perspectives*, 17, 119–140.

Mulheirn, I., & Pisani, M. (n.d.). Estimating the labor supply effect of the Working Tax Credit for childless households in the UK. Unpublished paper.

Neumark, D., & Wascher, W. (2001). Using the EITC to help poor families: New evidence and a comparison with the minimum wage. *National Tax Journal*, 54, 281–317.

Neumark, D., & Wascher, W. L. (2011). Does a higher minimum wage enhance the effectiveness of the Earned Income Tax Credit? *Industrial and Labor Relations Review*, 64, 712–746.

Rothstein, J. (2011). Is the EITC as good as an NIT? Conditional cash transfers and tax incidence. *American Economic Journal: Economic Policy*, 2, 177–208.

Scholz, J. K. (1994). The Earned Income Tax Credit: Participation, compliance, and antipoverty effectiveness. *National Tax Journal*, 47, 63–87.

Earned Income Tax Credit and Educational Outcomes

By Gordon B. Dahl, University of California San Diego

Introduction

One in five children in the U.S. live in families with incomes below the official poverty line. This fraction jumps to nearly one in three children when it includes families earning no more than 150% of the poverty threshold. These poverty rates are almost 50% higher compared to individuals age 18 to 64 and double that of those age 65 and older (U.S. Census Bureau, 2014). Given the large number of children growing up in low-income households, an important question is whether public policies aimed at reducing poverty can make a difference in a child's life. This article focuses on the Earned Income Tax Credit (EITC), which is currently the largest antipoverty program in the U.S.

The EITC is specifically targeted to bolster the finances of working families with children at the bottom of the income distribution. For example, a single mother with two children who earned \$15,000 in 2014 would have received an EITC benefit of \$5,450, which would push her family above the poverty line. In 2013, the EITC lifted 3.2 million children out of poverty and aided another 7.8 million children in low- to moderate-income households (Center on Budget and Policy Priorities, 2015).

Does the EITC Improve Educational Outcomes?

While there are many potential benefits of the EITC, and diverse possible consequences of growing up in poverty, this article focuses specifically on the relationship between EITC receipt and educational outcomes for children in the U.S. There are many reasons to think that poverty could adversely affect a child's academic success, and that income transfers through the EITC could play an important role in ameliorating substandard outcomes. Parents in poverty have higher levels of stress, depression, and poor health (Evans and Garthwaite, 2013; Milligan and Stabile, 2011). These pressures could limit parents' ability to nurture and support their children's academic development. Indeed, children from poor families lag behind their peers in verbal development and have more behavioral problems in the classroom (Parker, Boak, Griffin, Ripple, & Peay, 1999). Extra income has the potential to improve the home environment and a child's ability to succeed in school. Income transfers could also aid a child's development if extra money is spent on child-centered goods such as health care, books, quality daycare, or moving to a neighborhood with better public schools (Hoynes, Miller, and Simon, 2015; Jones, Milligan, and Stabile, 2015).

Until recently, however, the effects of poverty on children's educational achievement were unclear. Simple correlations reveal

that low-income students perform worse on standardized tests, are more likely to drop out of high school, and are less likely to attend and complete college (see, for example, Duncan and Murnane, 2011). But whether or not these observed associations are caused by low income has been questioned. The main concern is that children growing up in poor households may have worse home environments or other characteristics that the researcher does not observe. These omitted variables may be part of the reason for substandard achievement and may continue to affect a child's development even if extra income were transferred to these poor families. Looking at changes over time within a family is also problematic, as changes in family income could be associated with parental job loss, illness, or moving to a new neighborhood — all factors that could independently impact a child's performance in school.

Recent research leveraging the EITC has helped to clarify the debate, providing convincing evidence that income transfers from the EITC improve children's academic outcomes in both the short and long run. The EITC is a useful policy to examine how extra income can help children growing up in poverty. Changes to the EITC schedule translate into unexpected boosts to family income as well as an inducement for some parents to work additional hours (and therefore further increase family income). The emerging consensus is that the extra income provided by the EITC to low-income families has positive and sizable effects on children's academic achievement from as early as elementary school all the way up to college.

Short-Run Effects on Test Scores

Research by Dahl and Lochner (2012) used expansions in the federal EITC in the late 1980s and mid-1990s as exogenous sources of variation in family income. The largest of these changes increased the maximum EITC benefit by roughly \$2,900 (inflation adjusted to year-2015 \$), which translated into as much as a 20% increase in income for some families. Not only did the maximum benefit increase, but the income range that qualified for EITC payments also expanded. The idea underlying their estimation strategy is that the expansions affected families differentially based on the family's income before the EITC payment schedules increased in generosity. Their approach isolates changes in predicted income solely due to changes in the EITC schedule over time, avoiding the problem that shocks to family earnings might also be correlated with other factors that could influence child achievement.

Intuitively, if family income affects a child's cognitive achievement, then one should observe relative improvements in the test scores of children from the low- and moderate-income



families who benefited most from the EITC expansions. This is exactly what Dahl and Lochner found. Using a panel dataset of roughly 4,400 children from the National Longitudinal Survey of Youth (NLSY), they found that current income has a large impact on a child's academic performance. An extra \$1,000 in EITC income (year-2015 \$) increases combined math and reading test scores by 4.4% of a standard deviation. While these estimates are modest, they are encouraging. To help place this magnitude in perspective, the gap in test scores between children in families with more than \$78,000 in annual income (the 75th percentile) and children in families with less than \$30,000 (the 25th percentile) is roughly 75% of a standard deviation. A \$5,500 boost to income (the maximum EITC benefit during the sample period, adjusted for inflation to 2015 \$) reduces this test score gap by almost a third. Dahl and Lochner found larger effects for children growing up in the most disadvantaged families, boys, minorities, and younger children. Some of the increase in income could be driven by increased labor force participation of mothers. In terms of the dynamics of family income, they found that contemporaneous income has the largest impact, with smaller effects from past income, suggesting that recurring income transfers are needed to sustain higher achievement.

Is there a way to translate these short-term test score gains into improvements in future earnings? Chetty, Friedman, and Rockoff (2011) provide one approach. They first used Internal Revenue Service tax data combined with administrative data from a large school district to estimate the effects of the EITC and the Child Tax Credit (CTC) on child test scores in grades three to eight. They found similarly sized effects as Dahl and Lochner. Chetty et al. combined this with information on how test score increases associated with having a better teacher improve the probability of college attendance and earnings. They concluded that each extra dollar spent on the EITC and CTC increases the net present value of earnings by a little more than one dollar, due to the test score gains.

The emerging consensus is that the extra income provided by the EITC to low-income families has positive and sizable effects on children's academic achievement from as early as elementary school all the way up to college.

Long-Run Effects on Educational Attainment

An important question is whether the EITC has positive effects on educational outcomes later in life and not just when children are young. Three working papers discussed below suggest the answer is yes. These researchers identify two primary mechanisms by which EITC transfers could aid high-school

completion and college enrollment. First, sustained income transfers when children are young could improve school performance and therefore high-school completion and college readiness. Second, the EITC could serve as a form of financial aid to attend college. An important feature of the EITC is that for youth age 19 to 23 years old, it is a conditional cash transfer. To be a qualifying child for EITC payments, a youth must be either (i) younger than 19 or (ii) a full-time student and younger than 24. So, extra EITC income could both relax credit constraints and serve as an incentive to attend college.

"The EITC is the biggest return we get. It's impacted us because when it comes to my kids, that tax refund comes from my kids, so I give back to my kids. By that I mean they have a savings account and a part of the return goes into their college fund. I started that early so they can be prepared so it's established for them and things can be easier."

— Mother of two school-age children

Micheltmore (2013) used the differential timing and generosity of state EITC programs to study educational attainment. Twenty-six states and the District of Columbia currently offer their own EITC benefits on top of the federal EITC schedule. Except for Minnesota, states calculate eligibility and benefits as a percentage of the federal EITC credit, with the percentage ranging from a low of 3.5% to a high of 40%. Micheltmore used parents' education level as a proxy for EITC eligibility, and compared child outcomes before and after changes to state EITC benefits relative to children in non-implementing states. Using data from the Survey of Income and Program Participation, she found that a \$1,000 increase in the combined state and federal EITC maximum (year-2015 \$) results in a 1-percentage-point increase (i.e., a 4% increase) in full-time college enrollment among 18- to 23-year-olds and a 0.3-percentage-point increase (i.e., a 10% increase) in completion of a bachelor's degree. The effects are concentrated among children who were first exposed to state EITCs at younger ages.


Maxfield (2013) analyzed variation in maximum EITC payments driven by differences in the number of children in the family and the adoption of state-specific EITC programs. Using NLSY data, she first documented similar effects on contemporaneous math and reading test scores as Dahl and Lochner (2012) and Chetty et al. (2011). The novel part of the research looked at longer-term education outcomes. Maxfield found that a \$1,000 increase in the maximum EITC benefit (year-2015 \$) when a child is growing up translates into a 1.9-percentage-point increase in the probability of graduating from high school by age 19 and a 1.3-percentage-point increase in completing a year of college by age 19. The effects she found were larger for boys, minorities, and children who were younger during the EITC expansions.



Finally, Manoli and Turner (2014) used the shape of the EITC schedule and changes to it over time to study college enrollment rates. They took advantage of population-level tax data covering nearly all high-school seniors in the U.S. between 2001 and 2011. They found that a \$1,000 lump-sum EITC tax refund (year-2015 \$) in a child's senior year of high school increases college enrollment by approximately 0.5 percentage points. In contrast, there is no impact from an EITC-related refund in a child's junior year, which the authors interpreted as evidence that the EITC relaxes credit constraints.

Emerging Consensus

Taken together, the various studies robustly found that the EITC improves children's education outcomes. Several states, including Michigan, North Carolina, Oregon, Connecticut, and Kansas have recently debated whether to cut back their state EITC programs. In contrast, California just passed and Montana is considering implementing new EITC programs, and Illinois,

Massachusetts, Minnesota, Rhode Island, and Washington have proposed expanding their state EITCs. The best available research indicates the EITC is an effective policy tool and provides support for expansions over cuts. EITC transfers not only decrease poverty among low-income children and their families, but also yield sizeable educational gains in both the short and long run. 

References

- Center on Budget and Policy Priorities. (2015). *Policy basics: the Earned Income Tax Credit*.
- Chetty, R., Friedman J., & Rockoff J. (2011). *New evidence on the long-term impacts of tax credits* (IRS Statistics of Income White Paper).
- Dahl, G., & Lochner, L. (2012). The impact of family income on child achievement: evidence from changes in the Earned Income Tax Credit. *American Economic Review*, 102(5), 1927–1956.
- Duncan, G., & Murnane, R. (Eds.) (2011). *Whither opportunity? Rising inequality, schools, and children's life chances*. New York: Russell Sage.
- Evans, W., & Garthwaite, C. (2013). Giving Mom a break: The effect of higher EITC payments on maternal health. *American Economic Journal: Economic Policy*, 6(2), 258–290.
- Hoynes, H., Miller, D., & Simon, D. (2015). Income, the Earned Income Tax Credit, and infant health, *American Economic Journal: Economic Policy*, 7(1), 172–211.
- Jones, L., Milligan, K., & Stabile, M. (2015). *Child cash benefits and family expenditures: Evidence from the National Child Benefit* (NBER Working Paper No. 21101).
- Manoli, D., & Turner, N. (2014). *Cash on hand and college enrollment: Evidence from population tax data and policy nonlinearities* (NBER Working Paper No. 19836).
- Maxfield, M. (2013). *The effects of the Earned Income Tax Credit on child achievement and long-term educational attainment* (Working paper).
- Micheltmore, K. (2013). *The effect of income on educational attainment: Evidence from state Earned Income Tax Credit expansions* (Working paper).
- Milligan, K., & Stabile, M. (2011). Do child tax benefits affect the well-being of children? Evidence from Canadian child benefit expansions. *American Economic Journal: Economic Policy*, 3(3), 175–205.
- Parker, F., Boak, A., Griffin, K., Ripple, C., & Peay, L. (1999). Parent-child relationship, home learning environment, and school readiness. *School Psychology Review*, 28(3), 413–425.
- U.S. Census Bureau. (2014). *Income and poverty in the United States: 2013* (Current Population Reports P60-249).

The Earned Income Tax Credit's Impact on Health

By Peter S. Arno, PhD and Jeannette Wicks-Lim, PhD,
Political Economy Research Institute, University of Massachusetts, Amherst

Introduction

A longstanding and well-established literature has described a positive relationship between income and other measures of socioeconomic status such as wealth or education and health and well-being (Adler & Rehkopf, 2008; Marmot & Wilkinson, 2005; Braveman et al., 2005; Lantz et al., 1998). The Earned Income Tax Credit (EITC), a broad-based income support program that raises millions of Americans out of poverty, has been well covered by others in this issue. Examining the effect of changes in EITC benefits and their relation to health outcomes is especially useful in deepening our understanding of how income impacts health, because these policy changes can provide a source of income variation that is relatively exogenous to individual or household characteristics. Perhaps more



importantly, it provides an opportunity to broaden our views of both health and economic policy by exploring the relationship between them.

What is the evidence?

A small but growing body of research has begun to explore the relationship between higher income resulting from EITC benefits and improved health outcomes. This research generally has focused on maternal and child health outcomes because the vast majority of EITC benefits accrue to families with young children. These studies, based on a variety of different datasets, have mainly used a difference-in-differences analytic strategy around policy parameter changes to identify its impact on the health outcomes of individuals most likely to receive EITC benefits (e.g., single mothers with a high-school degree or less).

The difference-in-differences framework tries to isolate the impact of EITC benefits by comparing and contrasting the outcomes of two different groups over time — one that is “treated” with an injection of EITC benefits (e.g., through a policy expansion) and another group that is “untreated” and does not receive any additional EITC benefits. The “untreated” group is intended to control for any trend in the health outcome of interest that may be occurring at the same time but is unrelated to any EITC treatment. If the “treated” group experiences a change in its health outcomes that is notably different from the “untreated” group, this is attributed to the EITC “treatment.” Thus the label “difference-in-differences”: This approach identifies an EITC effect by measuring whether there is a *difference* in health outcomes over time between two *different* groups — those treated and those untreated.

Several studies have applied a quasi-experimental design using the large increases in EITC benefits occurring during the early and mid-1990s, embodied in the Omnibus Budget Reconciliation Acts of 1990 and 1993 (OBRA 90 & 93). In particular, these analyses take advantage of the fact that families with two or more children received a much larger boost in EITC benefits than other family types (i.e., families with no children or families with only one child) and try to link changes in health to these differently sized EITC benefit increases.

Kevin Baker (2008), in a widely cited but unpublished study, may have been the first to apply a difference-in-differences approach to estimate the changes from OBRA93. He found that the EITC both led to an increase in average birthweight and reduced the incidence of low birthweight. Boyd-Swan and

colleagues (2013) used this framework to estimate intent-to-treat health effects of the EITC with data from the National Survey of Families and Households. They found that the EITC expansion under OBRA90 generated health benefits for low-skilled mothers including lower depression symptomatology, an increase in self-reported happiness, and improved self-efficacy. Evans and Garthwaite (2014), using the OBRA93 expansions of the EITC, found an association between EITC benefits and maternal health outcomes. Combining data from the Behavioral Risk Factor Surveillance Survey (BRFSS) and the National Health and Nutrition Examination Survey (NHANES), they found improved self-reported mental and physical health and decreased biomarkers of physical and mental stress among mothers with a high-school degree or less. These findings are consistent with past research that indicates that low socioeconomic status affects health through stress or other related physiological conditions (Seeman et al., 2008; Kubzansky, Kawachi, & Sparrow, 1999).

EITC benefits improve the birthweights of newborns to single mothers with a high-school degree or less.



Hoynes, Miller and Simon (2015), also building upon the policy changes stemming from OBRA93, reported that EITC benefits improve the birthweights of newborns to single mothers with a high-school degree or less. They also considered the channels by which EITC benefits may improve low birthweight rates and found some evidence that increased EITC benefits raise the rate of prenatal care and reduce maternal smoking.

Some concerns have been raised in the literature regarding the short-term impact of income gains (as opposed to income) on health (Apouey & Clark, 2015; Evans & Moore, 2011; Phillips, Christenfield, & Ryan, 1999). Rehkopf and colleagues (2014) examined this phenomenon using 30 outcome measures from NHANES in the categories of diet, food security, health behaviors, cardiovascular biomarkers, metabolic biomarkers, and infection and immunity. They found that although EITC payments did not lead to universal health improvements, the overall effects were beneficial: “Indeed, many outcomes that are key determinants of health (e.g. food security, smoking/exposure to smoke) were affected in a health-promoting direction.” This finding is supported by several studies that have demonstrated that maternal smoking in particular is reduced in association with EITC receipt (Hoynes, Miller, & Simon, 2015; Averett & Wang, 2013; Cowan & Teffit, 2012), although some inconsistent results have also been reported with regard to smoking in low-income populations (Kenkel, Schmeiser, & Urban, 2014).

Other investigators have focused on the effects of state-level supplemental EITC programs on health outcomes. Strully and colleagues (2010) reviewed state programs that operated between 1980 and 2002 — up to 15 programs by 2002 — and found that the presence of state EITC programs produces higher average birthweights among single mothers with a high-school degree or less. They propose that this outcome results from the ability of small, short-term income increases to boost expectant mothers’ nutritional intake, mitigating prenatal poverty. (They also found that the EITC was associated with reduced odds of maternal smoking by about 5%.)

Baughman and Duchovny (2013) analyzed the health impacts of state programs on children’s health between 1992 and 2006, a period during which up to 20 states had adopted their own supplemental programs. They found that state EITCs are associated with improvements in health status for children ages 11 to 14, as reported by the child’s mother, concluding that this was due to higher rates of maternal employment and increased earnings.

“My health insurance doesn’t cover doctors visits but I have some EITC money left over and I can afford to get them checkups and deal with an emergency.”

— Mother of middle-school aged child

Our own study examined health effects of New York State’s and New York City’s EITC policies on low-income



neighborhoods between 1997 and 2010 (Wicks-Lim & Arno, 2015). We found that a 15-percentage-point increase in the EITC rates was linked to a 0.45-percentage-point reduction in the low birthweight rate in New York City's poor neighborhoods. This is substantial when we consider that low birthweight rates have fluctuated narrowly between 9.0% and 9.8% during that time period. The magnitude of our low-income neighborhood estimates suggests that EITC's impact on the low birthweight rate is stronger than that experienced by the average EITC-recipient household and falls within the range of traditional health policies such as Medicaid (Currie & Gruber, 1996). We speculate that because the conditions in high poverty neighborhoods appear to intensify poverty's impact on health and the EITC delivers benefits to residents in these areas in a concentrated way, it exerts an influence on individuals' health outcomes that is independent of an individual's own poverty status (Jacob, Ludwig, Douglas, & Miller, 2013; Kneebone & Berube, 2008; Brooks-Gunn, Duncan, & Aber, 1997).

What do the findings mean?


The evidence base supporting the link between income support policies such as the EITC and improved health outcomes is small, possibly because it has not been extensively studied, but the data are emerging and seem promising. The weight of the evidence, although not conclusive (Hammad & Rehkopf, 2015; Bruckner, Rehkopf, & Catalano, 2013; Pega, Carter, Blakely, & Lucas, 2013; Larrimore, 2011), suggests that the EITC does in fact improve health outcomes, particularly those affecting women and young children. However, there are still many gaps in our knowledge. We are far from a comprehensive understanding of the precise causal pathways between improvements in socioeconomic status and health outcomes. Additional research is needed to really know if improved health outcomes related to the EITC are the result of reduced smoking or stress, purchasing needed consumer goods or higher quality food, improving access to health care, or even enhanced neighborhood amenities.

There has always been a question of whether health improvements stemming from increased EITC benefits are the result of a direct income effect, from increased employment (which has been demonstrated in numerous studies; Wicks-Lim & Pollin, 2012; Adireksombat, 2010; Hotz & Scholz, 2010; Eissa & Hoynes, 2006; Meyer & Rosenbaum, 2001), or some combination of income and employment. Nichols and Rothstein (2015) have suggested that "The EITC effect should be interpreted to include effects operating through (for example) changes in time use, access to employer-provided health insurance, and the mental health consequences of employment." Clearly more research is needed to answer this question definitively. Yet from a public policy perspective, one has to ask, does it really matter? If employment rates and health status improve as a result of higher EITC benefits, where is the downside?

We also need to broaden our analytic framework to better understand the multiple and interactive levels at which socioeconomic status may affect health. As Patricia O'Campo (2013) stated in her aptly named chapter, *Harder Than Rocket Science? The Science of Designing and Implementing Strong Family-Friendly Policies*:

The dominant explanatory model used in epidemiologic and social epidemiologic inquiry continues to be the biomedical or "disease-specific model," which seeks to identify mostly individual-based risk markers and risk factors for specified health conditions. Thus, the study of macro-social policies and programs necessitates the expansion of the study designs used to understand and document contextual and macro-level influences on family and individual well-being.

If we are correct in our supposition of how the impact of the EITC operates in high-poverty neighborhoods, then its health effects may go beyond the income an individual may receive. By injecting millions of dollars into high-poverty communities, which in turn can generate additional economic activity (Haskell, 2006; Jacob France Institute, 2004), the EITC can have powerful, even community-wide, effects. This could be particularly important given the troubling fact that concentrated poverty has nearly doubled in this country between 2000 and 2013 (Jargowsky, 2015).

Finally, new research is required to go beyond single-issue analyses of the EITC and examine the potential joint impacts on health in various populations of other income support policies such as the Child Tax Credit and the minimum wage rate. The EITC-health nexus provides an opportunity to break down some of the silos between health and economic policy within the research community, as well as among funders and public officials. Perhaps the latest developments in neurobiology demonstrating the pernicious impact of poverty on normal brain development in children (Hair, Hanson, Wolfe, & Pollak, 2015) can strengthen our resolve to expand the social determinants of health's analytic framework to enhance our understanding of the social forces, institutions, and policies that can reduce poverty and improve our population's health 

References

- Averett, S., & Wang, Y. (2013). The effects of Earned Income Tax Credit payment expansion on maternal smoking. *Health Economics*, 22(11), 1344-1359. doi: 10.1002/hec.2886.
- Baker, K. (2008). *Do cash transfer programs improve infant health: Evidence from the 1993 expansion of the Earned Income Tax Credit*. Retrieved from <http://ntrda.me/1f0fxLi>
- Baughman, R. A., & Duchovny, N. (2013). *State Earned Income Tax Credits and the production of child health: Insurance coverage, utilization, and health status* (Working paper). University of New Hampshire.
- Boyd-Swan, C., Herbst, C. M., Ifcher, J., & Zarghamee, H. (2013). *The Earned Income Tax Credit, health, and happiness* (IZA Discussion Paper no. 7261). Bonn, Germany: Forschungsinstitut zur Zukunft der Arbeit. Retrieved from <http://ftp.iza.org/dp7261.pdf>

- Braveman, P. A., Cubbin, C., Egerter, S., Chideya, S., Marchi, K. S., Metzler, M., & Posner, S. (2005). Socioeconomic status in health research: one size does not fit all. *Journal of the American Medical Association*, 294(22), 2879–2888.
- Brooks-Gunn, J., Duncan, G. J., & Aber, J. L., (Eds.). (1997). *Neighborhood poverty volume 1: context and consequences for children*. New York: Russell Sage Foundation.
- Bruckner, T. A., Rehkopf, D. H., & Catalano, R. A. (2013). Income gains and very low-weight birth among low-income black mothers in California. *Biodemography and Social Biology*, 59(2), 141–156.
- Cowan, B., & Teffit, N. (2012). Education, maternal smoking, and the Earned Income Tax Credit. *The B.E. Journal of Economic Analysis & Policy*, 12(1), published online, doi: 10.1515/1935-1682.3305
- Currie, J., & Gruber, J. (1996). Saving babies: The efficacy and cost of recent changes in the Medicaid eligibility of pregnant women. *Journal of Political Economy*, 104(6), 1263–1296.
- Evans, W. N., & Garthwaite, C. L. (2014). Giving mom a break: The impact of higher EITC payments on maternal health. *American Economic Journal: Economic Policy*, 6(2), 258–290. doi: <http://dx.doi.org/10.1257/pol.6.2.258>
- Evans, W. N., & Moore, T. J. (2011). The short-term mortality consequences of income receipt. *Journal of Public Economics*, 95, 1410–1424.
- Hair, N. L., Hanson, J. L., Wolfe, B. L., & Pollak, S. D. (2015). Association of child poverty, brain development, and academic achievement. *Journal of the American Medical Association Pediatrics*. Published online, doi:10.1001/jamapediatrics.2015.1475
- Hammad, R., & Rehkopf, D. H. (2015). Poverty, pregnancy, and birth outcomes: A study of the Earned Income Tax Credit. *Paediatric and Perinatal Epidemiology*, In press. doi: 10.1111/ppe.12211
- Haskell, J. N. (2006). EITC boosts local economies. *Partners in Community and Economic Development*, 16(3), Federal Reserve Bank of Atlanta. Retrieved from <http://bit.ly/1OSS6n9>
- Hotz, J. V., & Scholz, J. K. (2010). Examining the effect of the Earned Income Tax Credit on the labor market participation of families on welfare. Unpublished manuscript. Retrieved from http://public.econ.duke.edu/~vjh3/working_papers/EITC2.pdf
- Hoynes, H. W., Miller, D. L., & Simon, D. (2015). Income, the Earned Income Tax Credit, and infant health. *American Economic Journal: Economic Policy*, 7(1), 172–211.
- Jacob, B. A., Ludwig, J., Douglas, L., & Miller, D. L. (2013). The effects of housing and neighborhood conditions on child mortality. *Journal of Health Economics*, 32(1), 137–150.
- Jacob France Institute. (2004). *The importance of the Earned Income Tax Credit and its economic effects in Baltimore City*. Baltimore, MD: The Jacob France Institute, University of Maryland.
- Jargowsky, P. A. (2015). *Architecture of segregation: civil unrest, concentration of poverty and public policy*. Century Foundation. Retrieved from <http://apps.tcf.org/architecture-of-segregation>
- Kenkel, D. S., Schmeiser, M. D., & Urban, C. (2014). Is smoking inferior? Evidence from variation in the Earned Income Tax Credit. *Journal of Human Resources*, 49(4), 1094–1120.
- Kneebone, E., & Berube, A. (2008). *Reversal of fortune: A new look at concentrated poverty in the 2000s*. Metropolitan Policy Program at Brookings. Retrieved from <http://bit.ly/1qCYBy5>
- Kubzansky, L., Kawachi, I., & Sparrow, D. (1999). Socioeconomic status and risk factor clustering in the normative aging study: Any help from the concept of allostatic load? *Annals of Behavioral Medicine*, 21(4), 330–338.
- Lantz, P. M., House, J. S., Lepkowski, L. M., Williams, D. R., Mero, R. P., & Chen, J. (1998). Socioeconomic factors, health behaviors, and mortality. *Journal of the American Medical Association*, 279(21), 1703–1708.
- Larrimore, J. (2011). Does a higher income have positive health effects? Using the Earned Income Tax Credit to explore the income-health gradient. *The Milbank Quarterly*, 89(4), 694–727. doi: 10.1111/j.1468-0009.2011.00647.x.
- Marmot, M., & Wilkinson, R. (2005). *Social determinants of health*. New York: Oxford University Press.
- O'Campo, P. (2013). Harder than rocket science? The science of designing and implementing strong family-friendly policies. In N. S. Landale, S. M. McHale, & A. Booth (Eds), *Families and child health* (p. 194). New York: Springer.
- Pega, F., Carter, K., Blakely, T., & Lucas, P. J. (2013). In-work tax credits for families and their impact on health status in adults. *Cochrane Database of Systematic Reviews*, Issue 8. Art. No.: CD009963. DOI: 10.1002/14651858.CD009963.pub2.
- Phillips, D. P., Christenfeld, N., & Ryan, N. M. (1999). An increase in the number of deaths in the United States in the first week of the month - an association with substance abuse and other causes of death. *New England Journal of Medicine*, 341, 93–98.
- Rehkopf, D. H., Strully, K. W., & Dow, W. H. (2014). The short-term impacts of Earned Income Tax Credit disbursement on health. *International Journal of Epidemiology*, 43(6), 1884–1894.
- Seeman, T., Merkin, S. S., Crimmins, E., Koretz, B., Charette, S., & Karlamangla, A. (2008). Education, income and ethnic differences in cumulative biological risk profiles in a national sample of US adults: NHANES III (1988–1994). *Social Science and Medicine*, 66(1), 72–87.
- Strully, K. W., Rehkopf, D. H., & Xuan, Z. (2010). Effects of prenatal poverty on infant health: state earned income tax credits and birth weight. *American Sociological Review*, 75(4), 534–562.
- Wicks-Lim, J., & Arno, P. S. (2015). *Improving population health by reducing poverty: New York's Earned Income Tax Credit* (Working Paper No. 377). Political Economy Research Institute. Retrieved from <http://bit.ly/1FIdVyc>
- Wicks-Lim, J., & Pollin, R. (2012). *Making work pay: Combining the benefits of the Earned Income Tax Credit and minimum wage*. Amherst, MA: Political Economy Research Institute. Retrieved from <http://bit.ly/1NVIUwM>

Earned Income Tax Credit, Savings and Child Outcomes

By Don Baylor, Urban Institute

Introduction

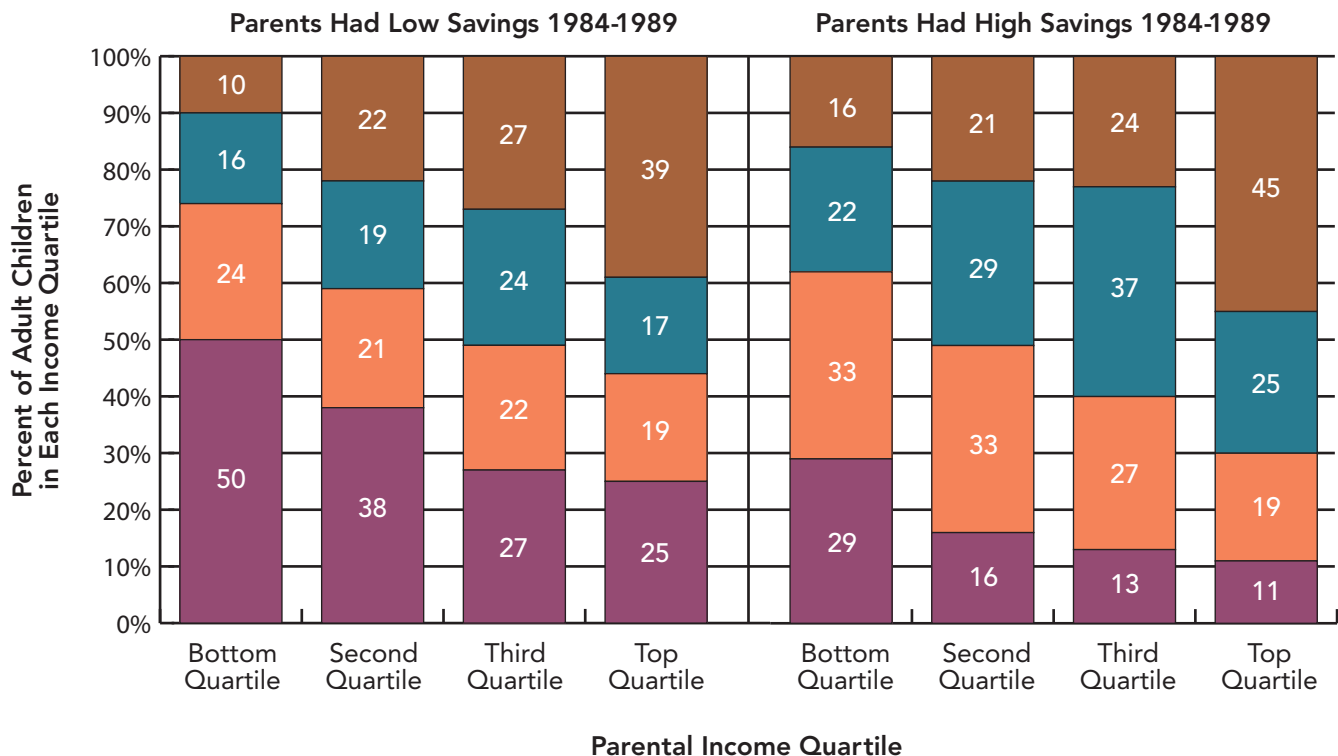
For those interested in child well-being, many policy areas and programs emerge that produce positive effects on households with children. Notably, early childhood development, quality K-12 education, health, nutrition, and youth enrichment programs receive a certain amount of attention and resources when one is seeking to “move the needle” on youth outcomes and break the cycle of intergenerational poverty. In recent years, the emergence of explicitly focused two-generation approaches has gained traction as research studies have confirmed how programs designed to lift incomes and build skills for adults also produce positive effects for children, creating something of a virtuous circle.

While the effects of income, neighborhood, and parental education—among other factors—on child well-being and economic mobility are widely known, recent evidence points to the positive effects of household assets upon child development.

Compared to their low-income peers without household savings, low-income children raised in households with a modest amount of savings are more likely to move out of poverty as adults (Cramer, O’Brien, Cooper, & Luengo-Prado, 2009). These “asset effects” are similar to those found with low-income children who complete higher education in terms of their chances for upward economic mobility. That is, household savings can play a significant role in breaking the intergenerational cycle of poverty.

Compared to their low-income peers without household savings, low-income children raised in households with a modest amount of savings are more likely to move out of poverty as adults.

Figure 1



Source: Pew Economic Mobility Project, 2009.

The importance of household savings, especially liquid assets, on child well-being has multiple explanations. For one, liquid savings, also known as precautionary or a rainy-day fund, can help families navigate an economic setback or fluctuation in income (Mills & Amick, 2010). Also, household savings can be leveraged for key asset-building activities such as home purchases, entrepreneurial investments, or higher education. Finally, liquid savings can play a role in preventing more households from taking out high-cost, short-term loans for immediate cash needs that can lead to asset stripping and deeper financial insecurity.

While more research is needed to pinpoint the savings “tipping point” for families and children, many stakeholders have begun to define financial vulnerability through the lens of liquid asset poverty. Liquid asset poverty is defined as the inability to cover three months of basic expenses upon a disruption in income initiated by a job loss or similar financial crisis. Over four in ten U.S. households lack such a safety net to navigate financial emergencies. Asset poverty rates are higher for families with young children, female-headed households, and African American and Latino families (Levin, 2014).

As the largest federal antipoverty program, the Earned Income Tax Credit (EITC) is a refundable tax credit geared toward low- and moderate-income households, and has been modified and expanded since its inception in 1975. This article seeks to explore the role of the EITC in providing a platform for economic security and mobility for lower-income families with children. Additionally, this essay will focus on the benefits of household savings for low-income families, the advent of the tax-time savings field, and how local, state, and federal policy choices affect EITC utilization as an asset-building platform. Finally, we will examine specific areas where further research and demonstrations are needed to shed light on promising practices and programs that further leverage the EITC for promoting economic mobility and family financial health.

The EITC as an Asset-Building Platform

In an era of income inequality, underemployment, and stagnant wages, the EITC plays an increasingly important role in promoting economic security. Since 1996, when Congress dramatically expanded the federal tax credit in tandem with welfare reform, the EITC has gained even greater clout, with several states and some cities enacting “piggyback” income tax credits. As of 2015, half of all states plus Washington, D.C., have enacted some type of a state EITC, with all but four of these measures being refundable. Additionally, Congress authorized a considerable increase with the 2009 American Recovery and Reinvestment Act and the 2012 American Taxpayer Relief Act. In tax year 2013, the federal EITC generated over \$66 billion in refunds. For that year, the average EITC refund totaled just over \$2,400 (Internal Revenue Service, 2014).

Because of its structure, the EITC is remarkably efficient in lifting families and children out of poverty. As shown by the relatively large refunds for low-wage earners, the EITC, along

with smaller refundable tax credits such as the Child Tax Credit, can represent a lump sum amount that could comprise 30% to 50% of a household’s annual net income. Overall, the EITC lifted 6.2 million individuals, including 3.2 million children, out of poverty in 2013 (Center on Budget and Policy Priorities, 2015). Certainly, states such as Maryland and New Jersey, with relatively generous EITCs of their own, are able to lift even more families with children above the poverty line.

In the earlier years of the refundable tax credit, educating and encouraging potentially eligible households to file for the credit proved to be a significant challenge. Given the profile of typical EITC filers, these refunds are more likely to be spent locally within the community, creating a sizable economic impact for local areas. To this end, the Internal Revenue Service (IRS) has operated the Volunteer Income Tax Assistance (VITA) to engage local governments, philanthropy, nonprofit organizations, employers, and faith-based organizations to coordinate and conduct outreach activities in order to maximize awareness and uptake of the EITC. The IRS provides training, equipment, and other resources for local organizations to do outreach and provide (free) federal income tax filing services for low-income populations.

Given the lump sum refunds earned by many lower-income households, community asset builders have viewed tax time as a key moment for household savings. Through the American Dream Demonstration, as well as the long track record of the federal Individual Development Account program, research had indicated that low-income families, many of whom were EITC-eligible, could save consistently over a multiyear period when focused on purchasing an asset (Corporation for Enterprise Development, 2009). However, little was known about how to encourage savings through the tax-time moment, whether for emergency savings or longer-term savings vehicles designed for education or retirement.

“It has helped tremendously. I’ve been able to save. I didn’t have to get a loan to purchase the new vehicle because of the EITC return. Next I’m saving for a down payment on a home. Saving is security. Having that emergency fund alone could keep them off the street. If I couldn’t work, I could still pay the rent and my bills.”

— Mother living on East coast

High-quality, accessible, and affordable tax preparation is an important platform for low-income families. Increasingly, organizations offering VITA services are leveraging the “tax-time moment” to embed savings, asset-building, and credit-building options for their clients. Finally, expanded tax preparation services have become even more important with the implementation of the Affordable Care Act (ACA), which directly links health care access with tax records, budgeting, and financial decisionmaking.



In 2014, VITA sites served over 3.2 million filers, generating \$3.9 billion in refunds, with about two thirds of filers receiving the EITC (Corporation for Enterprise Development, n.d.). Given its sizable role in the local economy every year, financial support for EITC outreach and VITA site activities has become a common strategy for municipalities, retailers, and nonprofit intermediaries such as local United Ways, and a cornerstone of strategies to increase economic security.

How Families Are Using the Tax-Time Moment to Build Savings

In the past decade, programs have emerged to leverage tax filing as a key opportunity for families to start savings, build assets, and get connected to other financial mainstream activities such as opening bank accounts, establishing a credit profile, or investing for the future. A small but important policy change emerged as a catalyst for tax-time savings when the IRS enabled filers to split refunds in 2007, with the option of purchasing U.S. Savings Bonds directly through the tax form. Largely because of the extensive VITA network, which had established itself as a trusted community resource and tax-time financial counselor, this policy change gave rise to a wave of demonstration projects to test successful strategies that encourage split refund-saving. Although many tax-time savings efforts have emerged since the implementation of Form 8888 — the IRS form to designate additional vehicles for refund deposit — this article will focus on two campaigns: Save USA and the OpportunityTexas Savings Bond Project.

Save USA: Largely considered the first large-scale demonstration for tax-time savings, Save USA initially launched with Save NYC, and expanded to three other sites. The project paired financial institutions with VITA to open savings accounts onsite, encouraged by a delayed 50% match if savers were able to maintain their original deposit for one year. For example, if an eligible taxpayer received a refund of \$3,000, the filer could choose to open a savings account with a \$500 deposit. If the filer maintained the \$500 balance without withdrawal, the saver would qualify for a \$250 match. Although these filers had access to the savings throughout the year, about two of three filers maintained their balance to qualify for the match. Given the oft-cited need for emergency savings and the need to “save for soon,” many observers considered the withdrawals to be a positive outcome as well, as it often precluded more expensive options such as high-cost payday or auto title loans to cover a shortfall or income volatility. Other communities such as Houston adopted similar programs, with many programs still in operation.

Texas “Baby Bonds”: Following the implementation of the split refund option, U.S. Treasury added the capability for tax filers to purchase U.S. Savings Bonds directly through the tax form. As these two refund options were enacted in 2007 and 2010, respectively, few VITA filers took advantage of this opportunity. Gradually, state and local VITA stakeholders began to experiment with efforts to encourage or incentivize their filers

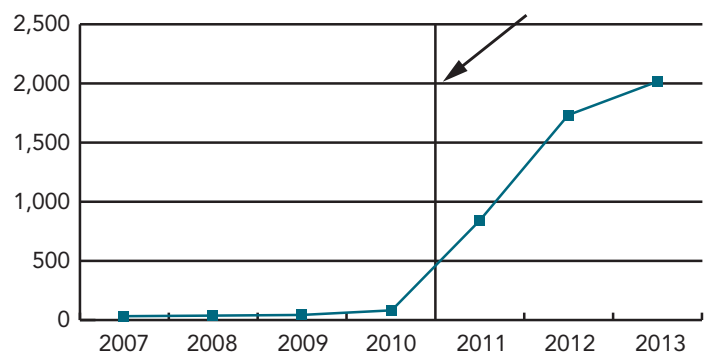
to take advantage of this opportunity. Statewide efforts included Alabama and many other local VITA stakeholders. However, the largest and longest organized grew out of Texas with the Opportunity Texas Savings Bond Incentive Project (2011–2015).

In 2011, the pilot year, OpportunityTexas partnered with the United Ways of Texas and Foundation Communities, an Austin-based VITA program, to test a series of questions about incentives, VITA filers, and long-term savings:

- What share of VITA filers might consider and actually purchase savings bonds?
- What was the right level and type of incentive?
- What were the best VITA techniques to facilitate bond purchases?
- What were major barriers to purchase?
- What were the main investment purposes for bond purchasers?

In 2010, the year prior to organized activity in Texas, fewer than 40 filers utilized Form 8888, or the split refund option. The below chart illustrates how the savings incentive intervention coincided with an uptick in split refunds at Texas VITA sites.

Table 3: Texas VITA Savers



Source: Neumark and Wascher (2011).

Over the course of the five-year program, a \$25 incentive produced about \$150 in savings, a 1:6 incentive-to-lump savings ratio.

Part of the project was to query filers about potential uses for their investments. Popular uses included education, retirement, and home purchase, while a significant share of filers purchased bonds for their children, particularly for postsecondary education (Mayo & Baylor, 2013).

Along with Save USA and similar projects, the Texas project yielded some important findings for the behavioral economics and savings field and put forth implications for grantmaking and public policy. Low-income filers expressed interest in both the security of having a rainy day fund and having an opportunity to build a nest egg for education, retirement, or other long-term

investments. Insofar as household savings — as important as a college degree — correlates strongly with upward mobility for children, philanthropy should examine ways to broaden access to modest household savings, whether for short-term or long-term uses.

Conclusion

For policymakers at the state and federal level, providing a platform and a default option are important for opening up access to millions of U.S. low-income filers. Connecting to default products for children's savings, retirement, or short-term savings would be an important intervention to reduce asset poverty, increase economic mobility, and improve financial health outcomes for low-income working families. Additionally, policymakers should revisit disincentives for liquid savings, namely asset limits for some public benefits. With the elimination of asset limits for the Children's Health Insurance Program and Medicaid through ACA implementation, state legislatures and agencies have an opportunity to streamline enrollment processes and empower families to become more economically resilient by eliminating asset tests for the Supplemental Nutrition Program and Temporary Assistance to Needy Families, as many states have already done.

For practitioners, further innovations are needed to ensure that savings interventions are timely, effective, and scalable. More experimentation is needed to uncover how technology (e.g., text messaging) can prime families for tax-time savings and developing the habit of household savings, especially short-term, liquid savings. Certainly, long-term savings products such as 529 college savings or general children's savings accounts are expanding, and should be more widely available in the direct service product portfolio.

For philanthropy, the strong findings that associate higher liquid savings with better financial outcomes for families and children should have meaningful implications for future grantmaking. While the tax-time savings demonstrations have indicated a desire for asset-building opportunities from low-income families, little is known about the financial outcomes for these families that have opted to save for the future or “save for soon.” Further research is needed to compare the well-being of tax-time savers against those families that declined the offer. ✨

References

- Center on Budget and Policy Priorities. (2015). Policy basics: The Earned Income Tax Credit.
- Corporation for Enterprise Development. (2009). American Dream demonstration overview.
- Corporation for Enterprise Development. (n.d.). Taxpayer Opportunity Network. Retrieved from http://cfed.org/programs/taxpayer_opportunity_network/advocacy_center/
- Cramer, R., O'Brien, R., Cooper, D., & Luengo-Prado, M. (2009). *A penny saved is mobility earned: Advancing economic mobility through savings*. Economic Mobility Project.
- Internal Revenue Service. (2014). Statistics for returns with EITC.
- Levin, E. (2014). *Saving up, moving up? Children, savings & opportunity*. Corporation for Enterprise Development Local Data Center.
- Mayo, A., & Baylor Jr, D. (2013). *A little goes a long way: Texas Community Tax Centers expand savings and services in 2013*. Center for Public Policy Priorities.
- Mills, G., & Amick, J. (2010). *Can savings help overcome income instability?* Urban Institute.



The Earned Income Tax Credit and Community Economic Stability

By Natalie Holmes and Alan Berube, Brookings Institution

For many in the United States, American poverty conjures images of urban blight or remote Appalachian hardship that motivated the War on Poverty in the 1960s. But the geography of poverty in the U.S. has shifted well beyond its historical confines (Kneebone & Berube, 2013). During the first decade of the 2000s, the poor population living in suburbs of the nation's largest metropolitan areas for the first time outstripped the poor population living in central cities, and poverty continues to grow faster today in the suburbs.¹ This trend has been even more pronounced for those living below twice the federal poverty line — equivalent to \$48,500 for a family of four in 2015 — which roughly mirrors the population eligible to receive the federal Earned Income Tax Credit (EITC).

Although it was not originally billed as an antipoverty program, in its 40 years, the EITC has become one of the nation's most effective tools for lifting low-income workers and their families above the poverty line. In 2013 alone, Brookings estimates that the EITC lifted 6.2 million people, including 3.1 million children, out of poverty (Kneebone & Holmes, 2014). What follows is a discussion of the EITC's growing importance to recipients in light of the new geography of poverty, its role in boosting local economies, and how expanding participation in the program and paying the credit differently could enhance its effectiveness as a local economic stabilizer.

The shifting geography of poverty challenges traditional approaches to combat poverty through investments in place.

When President Johnson declared a War on Poverty in 1964, poverty in the U.S. was primarily urban or rural. This was also the case in 1975 when the EITC was created: Nearly a million more low-income individuals at that time lived in rural areas or big cities than in the suburbs of major metropolitan areas.² Place-based antipoverty interventions dating to the War on Poverty were thus designed with these two geographies — especially cities — in mind. Brookings estimates that today, the federal government spends about \$82 billion per year across more than 80 place-focused antipoverty programs, spread across 10 agencies (Kneebone & Berube, 2013). Many are not well-suited to suburban contexts, for several reasons.

First, suburban poverty is more geographically diffuse than urban poverty. Suburban communities tend to be less densely populated than cities and larger in size, and cover more total area. Whereas centralized services might be appropriate in an

urban context because they are easily accessible to many in need, it is more difficult to achieve those economies of scale in the suburbs, where residents live farther apart and have limited access to transit. Many competitive federal grant programs allocate points based on population served and population density, implicitly favoring large central cities.

Second, suburban municipalities may lack the experience and administrative capacity needed to sustain services for low-income families and communities. Cities have dealt with poverty longer, and have had more time to develop strategies and structures to support their poor populations. Some of this capacity stemmed explicitly from Community Action Agencies, one of the original War on Poverty programs, which was intended to spur local innovation. Small suburban communities by and large did not have this same experience. Because of their relatively small size, suburban governments may not be able to achieve the administrative scale needed to deliver effective safety-net programs.

Third, many suburban communities lack the economic scale and fiscal structure needed to fund services for low-income residents. Because many small municipalities are limited in how they are permitted to raise revenues — typically through a combination of property and sales taxes — they are especially prone to financial instability caused by the very economic conditions that also generate greater need for services. As poverty suburbanizes, small suburban communities simultaneously face rising demand and falling tax revenues to support those services. Moreover, tax “competition” among many small suburbs within a metro area can further erode the fiscal capacity and political will for these jurisdictions to support people in need.

“It’s good just to have emergency money. Car repairs always come up at the worst time.”

— Mother of school-age child

¹ For the 100 largest Metropolitan Statistical Areas by 2010 population, we define “cities” as the first-named city in the metropolitan area title as well as any other title city with population over 100,000. “Suburbs” are defined as the metropolitan area remainder.

² Brookings analysis of decennial census data.

The new geography of poverty makes direct investments in low-income individuals and families — like the EITC — even more important.

The mismatch between existing place-based antipoverty strategies and the places where poverty is growing fastest heightens the importance of investing directly and effectively in low-income individuals and families through programs such as the EITC. Following its expansion in the mid-1990s, the EITC became the most significant cash transfer program available to low-income working families. The Internal Revenue Service (IRS, 2014) estimates that approximately 79% of EITC-eligible taxpayers nationally claim the credit each year — a remarkably strong participation rate among federal safety-net programs.

The high program participation rate and growth over time in EITC expenditures reflects both increases in the credit's generosity and growing need. In 2000, according to our analysis of IRS Stakeholder Partnerships, Education and Communities (IRS-SPEC) data, total EITC expenditures topped \$42 billion (in 2013 dollars). In 2013, they approached \$65 billion, equivalent to approximately 80% of the amount spent by the federal government on place-based poverty interventions.³

Analysis of IRS-SPEC data further suggests that the EITC's geographic incidence closely tracks the shifting geography of need. From 2000 to 2013, the number of suburban filers claiming the EITC rose by 62%, compared to 33% in cities. Changes in the distribution of EITC claims mirrored changes in the location of poor and near-poor populations, particularly growth in the suburbs.⁴ And because lower-income suburban communities (where at least 40% of residents are poor or near-poor) are becoming more diverse, too — 60% of their residents are non-White or Hispanic — the EITC also effectively reduces growing race-based income gaps in suburbs.⁵

EITC dollars support local economies.

The EITC benefits not only low-income families, but also the wider communities in which they live. Although it is widely regarded today as one of the country's most successful antipoverty programs, the EITC was originally designed to be a temporary economic stimulus measure, in the Tax Reduction Act of 1975 (Nichols & Rothstein, 2015). During the 2000s, more local and state governments made a concerted push to expand participation in the EITC among eligible filers, in part to inject more federal dollars into their local economies (Berube, 2006a).

There are several mechanisms through which the EITC could benefit local economies. California State University researchers categorize the local economic impact of EITC refunds as the sum of direct effects (EITC recipients spending their refunds), indirect effects (business spending in response to EITC recipient spending), and induced effects (changes in household income and spending patterns caused by direct and indirect effects). Together, these effects represent the local “multiplier” effect (Avalos & Alley, 2010). Their estimates for California counties

suggest that, in many cases, the credit creates local economic impacts equivalent to at least twice the amount of EITC dollars received.

Direct economic effects result from EITC recipients spending a portion of their refund locally, supporting local businesses and jobs. Consumer surveys show that low-income families spend a relatively large share of their income on groceries and other necessities, which tend to be purchased locally. Analysis of those surveys links tax refund season to increased likelihood of consumer activity as well as larger purchases (Adams, Einav, & Levin, 2009). People spend more, and more frequently, during tax refund season.

The EITC also supports local communities in less obvious ways. The concept of “tax incidence” reflects that the party being taxed, or receiving a tax credit, may not bear its full costs (or reap its benefits) because others shift their behavior in response to the tax. Along these lines, Jesse Rothstein estimates that as much as 36 cents of every dollar of EITC received flows to employers, because by enabling workers to better make ends meet on low wages, the credit effectively lowers the cost of labor. Those lower labor costs may, in turn, allow local employers to hire more local workers (Nichols & Rothstein, 2015).

Finally, emerging evidence suggests that progressive tax expenditures like the EITC can enhance intergenerational income mobility for local children, possibly by counteracting credit constraints that many low-income families face (Chetty, Hendren, Kline, & Saez, 2015). In areas with larger state EITCs, low-income children are more likely to move up the income ladder over time.

... emerging evidence suggests that progressive tax expenditures like the EITC can enhance intergenerational income mobility for local children, possibly by counteracting credit constraints that many low-income families face

The local impact of the EITC depends on how, and how many, eligible filers claim the credit.

The local impact of the EITC also depends on whether eligible workers and families file tax returns and claim the credit. As noted above, the IRS estimates that 79% of those eligible to receive the EITC nationally claim it. Given local variation in

³ The IRS-SPEC data from which these estimates are derived are available through Brookings' Earned Income Tax Credit Data Interactive: <http://www.brookings.edu/research/interactives/eitc>

⁴ We define the “near-poor” population as those with incomes below 200% of the federal poverty line, which is roughly equivalent to EITC eligibility.

⁵ Brookings analysis of American Community Survey data.



characteristics associated with uptake, there is likely also considerable local variation in EITC participation (Berube, 2005). Efforts to increase participation locally can thus increase the level of investment communities receive from the program.

Research has identified several factors associated with EITC participation rates among the eligible population. Eligible filers less likely to claim the credit include those who live in rural areas, are self-employed, do not have qualifying children, do not speak English well, are grandparents, or recently changed their filing status (IRS, 2015). One study suggests that communities with moderately sized immigrant populations may exhibit lower EITC participation rates, due perhaps to less robust social networks or more dispersed/heterogeneous populations that may limit awareness of the credit (Berube, 2006b).


Recent research also suggests that EITC participation is higher in areas with more tax preparers, who may promote greater local awareness of the credit (Chetty, Friedman, & Saez, 2012). While individuals who enlist the help of tax preparers are more likely to receive the EITC, they may face significant fees that blunt the credit's overall impact (Berube, 2006a). Expanding access to volunteer tax preparation services or simple, free online filing could help preserve more of the credit's value for low-income families and their communities.

To maximize the EITC's role as a local economic stabilizer, we should consider periodic payment options.

The EITC already functions as an important antipoverty tool for low-income workers and families, and a boon to local economic stability. Communities should nonetheless be interested in efforts to connect taxpayers to a portion of their EITC throughout the year, rather than only as a lump-sum refund at tax time.

Debt features significantly on the balance sheets of EITC recipients. Recent research finds that about 95% of EITC recipients have debt of some kind, and that large shares of refunds are dedicated to debt payments or deferred expenses (such as car repair). Recipients do not use the majority of EITC refunds to pay for monthly expenses, despite the fact that their wages typically cover only two-thirds of those expenses (Halpern-Meekin, Edin, Tach, & Sykes, 2015).

Paying a portion of filers' anticipated EITC periodically (and directly, rather than through employers like the defunct Advance EITC program) in smaller amounts over the course of a year could help them cope with these spending constraints and avoid taking on debt (Holt, 2008). By enabling families to better keep up with spending on regular items most often purchased locally — rent, food, vehicle maintenance — periodic payments could also support local economies. And by improving families' liquidity, such payments could reduce reliance on high-cost financial products such as payday loans.

The EITC continues to gain importance as place-based strategies lag behind poverty's suburbanization, and communities seek ways to maximize public investment in the face of budget constraints at all levels. The program lifts millions of working individuals and families out of poverty each year regardless of their location, and in doing so also supports community financial stability. An expanded EITC — at the federal, state, or local level — with options for periodic payment and better alternatives to high-cost tax preparation could provide even stronger support to low-income families and the places where they live. 

References

- Adams, W., Einav, L., & Levin, J. (2009). Liquidity constraints and imperfect information in subprime lending. *American Economic Review*, 99(1), 49–84. Retrieved from <http://web.stanford.edu/~jdlevin/Papers/Liquidity.pdf>
- Avalos, A., & Alley, S. (2010). The economic impact of the Earned Income Tax Credit (EITC) in California. *California Journal of Politics and Policy*, 2(1). Retrieved from <http://escholarship.org/uc/item/2jj0s1dn>
- Berube, A. (2005). *Earned income credit participation—What we (don't) know*. Washington, DC: Brookings Institution. Retrieved from <http://www.brookings.edu/metro/eitcparticipation.pdf>
- Berube, A. (2006a). *Using the Earned Income Tax Credit to stimulate local economies*. Washington, DC: Brookings Institution. Retrieved from <http://www.brookings.edu/~media/research/files/reports/2006/11/childrenfamilies-berube/berube20061101eitc.pdf>
- Berube, A. (2006b). *¿Tienes EITC? A study of the Earned Income Tax Credit in immigrant communities*. Washington, DC: Brookings Institution. Retrieved from http://www.brookings.edu/~media/research/files/reports/2005/4/childrenfamilies-berube02/20050412_tieneseitc.pdf
- Chetty, R., Friedman, J., & Saez, E. (2012). *Using differences in knowledge across neighborhoods to uncover the impacts of the EITC on earnings* (NBER Working Paper Series no. 18232). Retrieved from <http://eml.berkeley.edu/~saez/chetty-friedman-saezNBER13EITC.pdf>
- Chetty, R., Hendren, N., Kline, P., & Saez, E. (2015). *The economic impacts of tax expenditures: Evidence from spatial variation across the U.S.* Retrieved from <http://www.irs.gov/pub/irs-soi/14rpttaxexpenditures.pdf>
- Halpern-Meekin, S., Edin, K., Tach, L., & Sykes, J. (2015). *It's not like I'm poor: How working families make ends meet in a post-welfare world*. Oakland, CA: University of California Press.
- Holt, S. D. (2008). *Periodic payment of the Earned Income Tax Credit*. Washington, DC: Brookings Institution. Retrieved from <http://www.brookings.edu/research/papers/2008/06/0505-metroraise-supplement-holt>
- Internal Revenue Service. (2014). Statistics for tax returns with EITC. Retrieved from <http://www.eitc.irs.gov/EITC-Central/eitcstats>
- Internal Revenue Service. (2015). About EITC. Retrieved from <http://www.eitc.irs.gov/EITC-Central/abouteitc>
- Kneebone, E., & Berube, A. (2013). *Confronting suburban poverty in America*. Washington, DC: Brookings Institution Press.
- Kneebone, E., & Holmes, N. Fighting poverty at tax time through the EITC. Retrieved from <http://www.brookings.edu/blogs/the-avenue/posts/2014/12/16-poverty-tax-eitc-kneebone-holmes>
- Nichols, A., & Rothstein, J. (2015). *The Earned Income Tax Credit (EITC)* (NBER Working Paper Series no. 21211). Retrieved from <http://www.nber.org/papers/w21211.pdf>

Conclusion

By Patrick McCarthy, The Annie E. Casey Foundation

This year marks the 40th anniversary of one of the most effective poverty-reduction tools in the nation's history: the Earned Income Tax Credit (EITC). Both the anniversary and the critical policy debates likely to continue throughout the presidential election cycle make this a propitious moment to reflect on the EITC's impact on America's families, and to examine which policies and programs are working to advance opportunity for all.

I commend the EITC Funders Network; Grantmakers for Children, Youth and Families; and Grantmakers Income Security Taskforce cross-systems look at the EITC. In doing so, they have highlighted its role in creating a buffer for low-wage families today — and in providing ladders of opportunity for the children living in low-income families who receive the tax credit.

Indeed, when the Annie E. Casey Foundation began supporting federal and state EITC policies in 1994, we did so because of a commonsense conviction that children do well when their families do well. Today, the EITC lifts more children out of poverty than any other antipoverty program. This is good news, as we have long known that growing up in poverty affects a child's life chances. When we began to work on the EITC, we were compelled by its ability to increase incomes for poor families with children — and especially to help struggling low-wage workers to make work pay for them and their children. We worked hard with advocacy partners to amplify the power of the federal EITC by creating state versions of the tax credit and ensuring those state EITCs were structured as a refundable credit, giving families with no tax liabilities the credit as a refund. Today, 26 states and the District of Columbia have enacted their own EITCs, providing an additional income boost to millions of families working hard to make ends meet.

Recent research in anthropology and other social sciences, as well as new findings in neuroscience, highlights the ways in which the lack of income, especially early in a child's life, casts a long shadow on the lives of children, impacting their education, work, and health outcomes for decades to come. Through this research, much of which is cited in this volume, we have begun to learn more about the impact of the EITC on families' well-being today — and on their children as they grow. We know the EITC is critical to helping families cover their basic needs, but it also helps them weather the unexpected, such as expensive car repairs or emergency health care costs. Equally important, we are beginning to see the EITC's impact on the lives of the children in families receiving this credit. In effect, the EITC provides a

great example of a two-generation policy solution — one that benefits the adults receiving the credit while also improving their children's own circumstances later in life.

With the increasing body of research pointing to the role of income in and of itself in fostering the well-being of families and children, the EITC stands out as one of the most effective tools. For example, researchers Greg Duncan and Katherine Magnuson suggest that increasing family incomes by just \$3,000 to \$4,000 can have a significant impact on what their children later earn when they enter the workforce. Their findings seem especially true when that extra income is available to families with young children (up to age 3), suggesting that income boosts during these early years can have long-term payoffs.¹ Researchers hope to embark on a more rigorous test of the effects of income on very young children to better understand exactly how this additional income boosts child well-being. In the meantime, the EITC and other refundable credits, especially the Child Tax Credit, continue to help parents and their children succeed together.

In our recent report, *Creating Opportunity for Families: A Two-Generation Approach*², we highlight several policies that could help address the needs of parents and children simultaneously so that both can succeed. The report documents why more of our policy efforts should be focused on programs and tools that help families with very young children achieve financial stability from the beginning, avoiding the stressors, strains, and adversity associated with poverty that in turn lead to poor educational, health, social, and economic outcomes for their children. Moreover, we know that better aligning policies, programs, and public systems focused on adults with those focused on children increases the odds of success for parents and their children. We need to learn more, but investing in efforts with this double-bottom-line benefit for parents and children should be a driving focus of federal, state, and local policymakers.

The chapters in this volume provide compelling evidence of the many positive effects the EITC has on adults and children. As Natalie Holmes and Alan Berube note in their chapter, the credit continues to help low-income communities as it was

¹ Duncan, G. J., & Magnuson, K. (2011, Winter). The long reach of childhood poverty. *Pathways*, 22–27.

² Annie E. Casey Foundation (November 12, 2014). *Creating Opportunities for Families: A Two-generation Approach*. <http://www.aecf.org/m/resourcedoc/aecf-CreatingOpportunityforFamilies-2014.pdf>



originally designed to do, providing a multiplier effect of at least twice the value of the credit in communities. David Neumark's chapter highlights the impacts of the credit on employment and how it has helped make work pay in an era when wages at the bottom of our economy have stagnated. Across the political divide, there is widespread agreement that a job is one of the best pathways out of poverty. The EITC makes good on that belief by supplementing low wages, and Neumark notes that efforts to make the EITC more generous are a proven step to addressing rising income inequality.

Peter Arno and Jeannette Wicks-Lim's chapter points out that the benefits also extend to the health and well-being of parents and children; parents were less likely to suffer from depression, and their children were less likely to be born at low birthweight. As they point out, new neurobiology findings increasingly point to the harmful effects of poverty on children's brain development. In his chapter, Don Baylor highlights how many families have used the EITC to build assets — as he notes, to “save for soon” and also to “save for later” investments such as college, retirement, or home purchases. Finally, Gordon Dahl outlines some of the long-term impacts of the EITC — not just as a safety net for low wages but also as a ladder of opportunity for children in low-income families. As he points out, children whose parents have access to higher EITCs have better test scores in elementary school and a greater likelihood of graduating from high school and completing college.

Indivar Dutta-Gupta and Kali Grant remind us that all of the EITC's benefits help address rising inequality and serve as a prime policy driver in “insuring against the vicissitudes of life.” Indeed, they note that in other nations, lower levels of income inequality lead to longer periods of economic growth and expansion — which means policies like the EITC benefit all of us, not just low-income families. But their chapter also cautions that the EITC is no panacea for income inequality — and that we should put it into a larger context of the skills and tools that low-income families need so that they and their children can thrive in today's economy.

Charting a Path Forward

While the Earned Income Tax Credit has been one of the nation's most successful antipoverty programs, we can still do more to help families move out of poverty and create opportunities for children in low-income families to rise above their circumstances. As Robert Greenstein points out, a first critical step is making sure the program continues, as it began, as a thoroughly bipartisan solution. As these chapters show, the benefits across health, education, asset building, and community development should ensure that policymakers from both parties continue to point to the benefits of EITC and work together to protect, improve, and expand upon its success.

While the Earned Income Tax Credit has been one of the nation's most successful antipoverty programs, we can still do more to help families move out of poverty and create opportunities for children in low-income families to rise above their circumstances.

While nearly 80% of families who are eligible for the credit claim it, that still leaves about 20% — more than 7 million workers and their families — who don't get this vital boost to their income even though they are eligible for it. We can and must do more to ensure that those who qualify for the tax credit actually receive it.

To that end, we in the philanthropic community can join forces with government and nonprofits to provide free tax-preparation assistance and foster a no-wrong-door approach to helping families access the credit. This means reaching out to find eligible families in our schools, in the workplace, in community centers, in health clinics, and in our churches, synagogues, and mosques. We simply cannot afford to leave an estimated \$18 billion of financial support for workers, their families and their communities on the table each year.³

For far too many families, their most likely provider of help to access the EITC is a paid tax preparer instead of free tax assistance. So we must also continue to push for regulations of this industry to ensure that working families receive the credits they have earned. As many in this volume note, we must redouble all of these efforts — especially in suburban communities with less infrastructure for accessing public programs and support services — so that families can get this much-needed credit.

There are also opportunities to expand the EITC for those who don't qualify for the full credit. In particular, extending the credit to low-wage workers without children living in their household could dramatically increase its reach. Early evidence from similar efforts suggests that a change in the EITC could improve labor force participation and earnings, marriage rates, and child well-being (through noncustodial parent earnings). The Casey Foundation is supporting a rigorous demonstration of the effects of this type of expansion, called Paycheck Plus, and we are encouraged that presidential candidates from both major parties are actively supporting such an expansion.

³ Author's calculations.



Natalie Holmes and Alan Berube note that because the EITC is delivered in one lump sum during tax season, it can prevent families from using the credit's refund for basic ongoing needs. While prepayment of the credit has been tried before, with disappointing take-up, it is time to again identify new ways to provide a portion of an anticipated EITC refund throughout the year. This could help families make ends meet and balance earnings over 12 months — something the unpredictable low-wage labor market often does not provide for families.

These chapters highlight several other innovative ideas that are worthy of consideration. First, as the authors have noted, the earlier families with young children gain additional income, the better children do later in life. Increasing a worker credit for parents of very young children — especially those younger than 3 — would mitigate the high costs of having a baby and potentially lead to long-term benefits for their children. This baby bonus, delivered either through the EITC or the Child Tax

Credit, could help ensure that children's growth and development are not undermined by their families' economic circumstances.

The chapter on education and asset building also calls for more innovations on how the EITC can use the best thinking from behavioral economics to incentivize savings and college attendance among children in low-income families. Research shows that having the EITC starting earlier in their life helps keep kids on track to graduate from high school and attend college, so efforts to boost incomes when children are young will likely further support them in achieving these educational goals. In other asset-building efforts, parents of all incomes are beginning to save early for college through 529 Plans, and some communities have set up matched Children's Savings Accounts to encourage saving for children's future needs. Policymakers should look for innovative ways to connect EITC refunds to these saving mechanisms to further the credit's impact on educational attainment.

In the end, we know that allowing families to keep more of their income is critical to their financial stability. We must redouble our efforts to build on the EITC's success and continue to ensure that it — along with other policies addressing inequality — helps low-income families meet basic needs now while also laying the foundation to support their children's long-term success. Broad and continued support for this important antipoverty tool honors our core belief that in America, where a child starts out in life should not determine where he or she ends up. For the millions of children growing up in low-income families today, the climb out of poverty remains steep. The EITC is essential to giving parents the boost they need to provide opportunity to the next generation. ✨

Acknowledgments

Grantmakers for Children, Youth and Families, the Grantmakers Income Security Taskforce and the EITC Funders Network would like to acknowledge and thank the following individuals for sharing their insights, expertise, and time to produce this issue of *Insight*:

Writing & Editing:

- Peter Arno, Senior Fellow and Director of Health Policy Research, University of Massachusetts, Amherst
- Don Baylor, Senior Associate, Urban Institute
- Alan Berbube, Senior Fellow and Deputy Director, Metropolitan Policy Program, Brookings Institution
- Natacha Blain, Associate Director/Acting Executive Director, Grantmakers for Children, Youth and Families
- Gordon Dahl, Professor, Department of Economics, University of California, San Diego
- Indivar Dutta-Gupta, Director, Project on Deep Poverty and Senior Fellow, Georgetown University Law Center on Poverty and Inequality
- Kali Grant, Program Assistant, Project on Deep Poverty, Georgetown Center on Poverty and Inequality
- Robert Greenstein, Founder & President, Center on Budget and Policy Priorities
- Natalie Holmes, Senior Research assistant, Metropolitan Policy Program, Brookings Institution
- Patrick McCarthy, President & CEO, Annie E. Casey Foundation
- LaJune Montgomery Tabron, President & CEO, W.K. Kellogg Foundation
- Ami Nagle, President, Nagle & Associates
- David Neumark, Professor of Economics and Director, Center for Economics & Public Policy University of California, Irvine
- Janette Wicks-Lim, Assistant Research Professor Political Economy Research Institute, University of Massachusetts, Amherst
- Michelle Quirk, Editor

Advisory Committee

- Tony Banegas, former Philanthropic Advisory-Programs, Arizona Community Foundation
- Patrick Hain, Program Associate, Center for Community and Economic Opportunity
- Jennifer Lockwood-Shabat, President & CEO, Washington Area Women's Foundation
- Yanique Redwood, President & CEO, Consumer Health Foundation
- Paula Sammons, Program Officer, W.K. Kellogg Foundation
- Ada Schanez, Executive Director, Peppercorn Foundation
- Shelley Waters-Boots, Senior Consultant, Annie E. Casey Foundation

Stories

- Center for American Progress

Design & Production

- ImagePrep Studio

This publication is supported by the Annie E. Casey Foundation.



Grantmakers for Children, Youth & Families

8757 Georgia Avenue, Suite 540

Silver Spring, MD 20910

p 301-589-GCYF

f 301-589-4289

info@gcyf.org

www.gcyf.org