

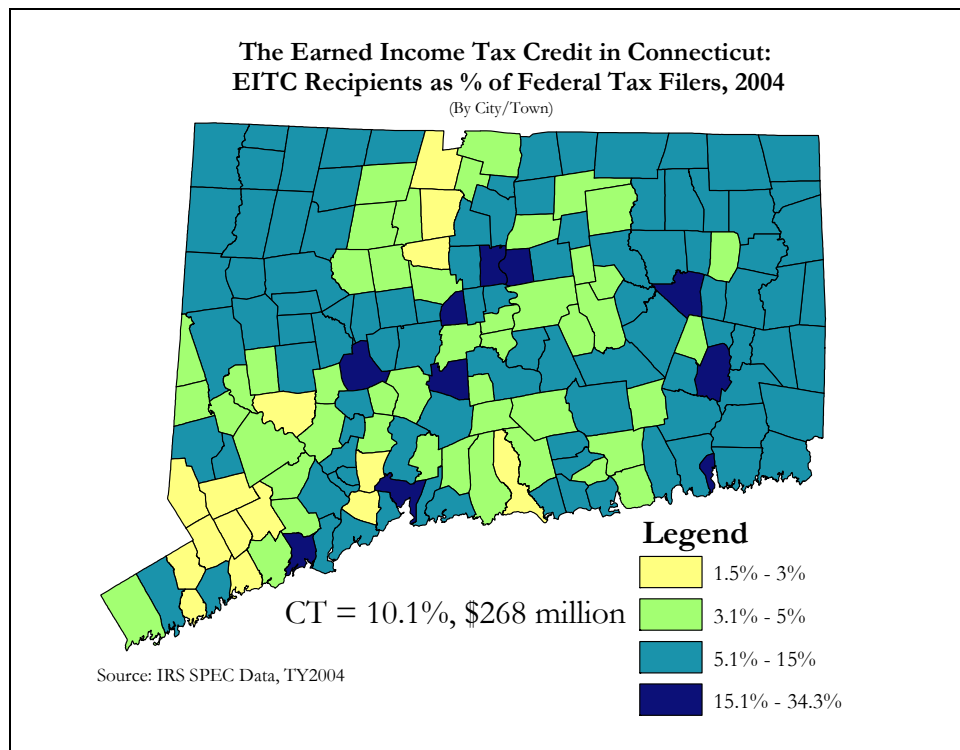


The Earned Income Tax Credit – What It Does For CT, And How It Could Do Much More

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The federal Earned Income Tax Credit (EITC) is a tax credit available to low-income working families. If their income tax liability is less than the amount of the credit, the difference is paid to the family (thus it is *refundable*). The EITC reduces taxes and supplements wages for low-income families who are working.

The federal EITC lifts more children out of poverty than any other federal program. Roughly one in six families in the United States files a tax return that claims the federal EITC. Each year, the credit helps lift more than 4 million people out of poverty; roughly half of these people are children.



The federal EITC benefits thousands of families in CT. In 2004, 165,000 families in CT claimed the federal EITC, bringing \$268 million into the pockets of Connecticut's lower wage working families. The proportion of CT families claiming the federal EITC is as high as 50% in some zip code areas. Statewide, about 10% of CT tax filers collected the EITC in 2002, 2003, and 2004.¹ EITC claimants live in every Connecticut town.

¹ The federal EITC could do even more. In 2004, federal EITC claimants lost \$1.6 billion of their credits to fees and high interest rates on Refund Anticipation Loans. While 4.5% of all federal income tax filers in Connecticut used RALs in 2004, the rate amongst EITC recipients was much higher, at 24.1%. Also, not everybody who is eligible for the federal EITC has been collecting it. The IRS estimates that only 70% of eligible filers in Connecticut are claiming the federal EITC. If the remaining 30% participated in the program,

Each of Connecticut's neighboring states has a *state* EITC. Currently, 20 states (including Massachusetts, Rhode Island, New York, New Jersey, and Vermont) and two local governments have an EITC. These supplemental EITCs lift even more families out of poverty, while providing additional economic stimulus for local and state economies.

A Connecticut EITC would help low-income families achieve economic self-sufficiency. *The EITC rewards work* and targets the 'benefit cliffs' where full time work cannot achieve income adequacy. Connecticut's self-sufficiency standard, which provides a more realistic assessment of the costs faced by Connecticut parents raising children, shows that for families in every region of the state, economic self-sufficiency requires a much higher annual income than the federal poverty level.² Yet Connecticut's state income tax makes no allowance for the costs of child rearing (such as by providing a deduction for dependents). A Connecticut EITC would help address this inequity and help families make ends meet.

A Connecticut EITC would address the growing disparity between high- and low- wage earners. Between 1990 and 2005, Connecticut wage earners at the 10th percentile saw their real wages decline by 3%, while wages of the earners at the 90th percentile increased by 19%.³

A Connecticut EITC would make our tax system more fair. Connecticut's poorest families pay more than twice the proportion of their income in state and local tax than do the state's most affluent families. While most of the Connecticut families who are eligible for the federal EITC have no current state income tax liability, all pay sales and property taxes (either directly if they own a home or car, or indirectly through rent). Among all states, Connecticut's income tax threshold (the point at which families start paying taxes) has seen the greatest erosion compared with the federal poverty level (FPL) since 1991, declining from 71% over the FPL to just 21% over the FPL in 2005. In fact, Connecticut is now the only state with an income tax that has not increased its tax threshold since 1991. This, coupled with the failure to enact a state EITC, has increased the relative regressivity of Connecticut's overall taxes for low income families. In tax year 2005, a Connecticut family earning \$15,577/year owed \$0 in state income tax while the same family, in Vermont, received a \$1,327 tax refund.⁴

A Connecticut EITC would NOT be subject to the state spending cap. The EITC, including any refundable portion (that which exceeds the family's income tax liability), is an adjustment to revenue, rather than an appropriated expenditure, and therefore not subject to spending cap limitations.⁵

A CT EITC would further stimulate Connecticut's local economies. A state EITC would be both an effective and economically efficient way to boost consumer spending. Studies show that when families receive their federal EITC checks, funds are quickly re-invested in the economy (e.g. though payment of overdue bills).

The EITC has enjoyed broad bipartisan support since its inception. Enacted in 1975 under President Ford, the federal EITC has been expanded under several administrations. Ronald Reagan referred to the federal EITC as "the greatest anti-poverty measure." President George H.W. Bush and President Bill Clinton also praised the EITC and both proposed expansions to the federal program during their presidencies.⁶

Connecticut's low-income working families would receive an additional \$100 million. Dan Haar, "Income Tax Credit Going Unclaimed," *Hartford Courant*, January 30, 2005.

² Diana Pearce, *The Real Cost of Living in 2005: Self-Sufficiency Standard for Connecticut* (prepared for the State of Connecticut Office of Workforce Competitiveness, December 2005).

³ Douglas Hall and Shelley Geballe, *The State of Working Connecticut, 2006* (Connecticut Voices for Children, 2006).

⁴ Nicolas Johnson, Bob Zahradnick and Joseph Llobrera, *State Income Tax Burdens on Low-Income Families in 2002* (Center on Budget and Policy Priorities, 2003).

⁵ The precedent for this treatment of refundable tax credits has been established by the treatment of the partially refundable Research and Development and Research and Experimentation credits against the corporation business tax. See *Connecticut Tax Expenditure Report 2004*, Connecticut General Assembly, Office of Fiscal Analysis, p. 78.

⁶ Robert Greenstein, *The Earned Income Tax Credit: Boosting Employment, Aiding the Working Poor* (The Center on Budget and Policy Priorities, 2005).