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The Earned Income Tax Credit (EITC) is a federal tax credit for low- and moderate-income working people. It is designed to encourage and reward work as well as offset payroll and income taxes. The EITC is “refundable,” which means that if it exceeds a low-wage worker’s income tax liability the IRS will refund the balance. Twenty-four states have established their own EITCs to supplement the federal credit.

Who Is Eligible, and for How Much?

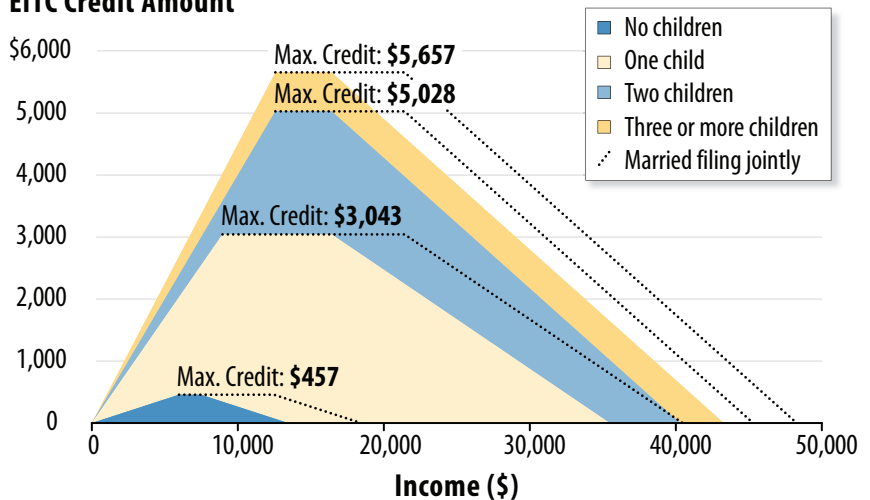
Working families with children that have annual incomes below about \$35,000 to \$48,000 (depending on marital status and the number of children in the family) generally are eligible for the federal EITC. Also, working poor people without children that have incomes below about \$13,000 (\$18,000 for a married couple) can receive a very small EITC.

A recent study found that half of all families with children receive the EITC at some point. In the 2007 tax year alone, some 25 million working families and individuals received the EITC. The amount of EITC depends on a recipient’s income, marital status, and number of children. As shown in the figure, workers receive the credit beginning with their first dollar of income.

The amount of the credit rises with income until it reaches a maximum level and then begins to phase out at higher income levels. In 2007, the average EITC was \$2,488 for a family with children and \$243 for a family without children. .

The Federal Earned Income Tax Credit in Tax Year 2009

EITC Credit Amount



Note: Married couples with income in the phaseout range qualify for a higher credit than singles—shown by dashed lines.

Policy Basics is a series of brief background reports on issues related to budgets, taxes, and government assistance programs.

The Center on Budget and Policy Priorities
 820 First Street, NE, Suite 510
 Washington, DC 20002
 Ph: 202-408-1080
 Fax: 202-408-1056
 center@cbpp.org
<http://www.cbpp.org>

Research indicates that families use the EITC to pay for necessities, repair homes, maintain vehicles that are needed to commute to work, and in some cases, obtain additional education or training to boost their employability and earning power.

Encouraging and Rewarding Work

The EITC is designed to encourage and reward work. Beginning with the first dollar, a worker's EITC grows with each additional dollar of wages until it reaches the maximum value. This creates an incentive for people to leave welfare for work and for working poor people to work additional hours towards full-time employment.

This incentive feature has made the EITC remarkably successful. Studies have shown, for example, that the EITC has encouraged large numbers of single parents to leave welfare for work. The Committee for Economic Development, an organization of 250 corporate executives and university presidents, concluded in 2000 that "The EITC has become a powerful force in dramatically raising the employment of low-income women in recent years."

Reducing Poverty

In 2009, the EITC lifted an estimated 6.6 million people out of poverty, including 3.3 million children. The poverty rate among children would have been nearly one-third higher without the EITC. The EITC lifts more children out of poverty than any other single program or category of programs.

One way the EITC reduces poverty is by supplementing the earnings of minimum-wage workers. There is broad bipartisan agreement that a two-parent family with two children with a full-time, minimum-wage worker should not have to raise its children in poverty. At the minimum wage's current level, such a family can move out of poverty only if it receives the EITC as well as food stamps.

Strengthening the EITC

The American Recovery and Reinvestment Act of 2009 (ARRA) expanded the EITC in two ways. First, ARRA added a "third tier" of the EITC for families with three or more children. These larger families can now receive \$629 more than families with only two children. This addition recognizes the reality that larger families face a higher cost of living and that families with three or more children are more than twice as likely as smaller families with children to be poor. Second, ARRA expanded marriage penalty relief in the EITC, reducing the financial penalty some couples receive when they marry by allowing married couples to receive larger benefits. These two expansions together benefited over 7 million people, and kept over 3 million people out of poverty.

While major improvements in the short term, these key provisions are scheduled to expire at the end of 2010 if Congress does not take action. Additionally, the EITC for workers without children remains extremely small — too small even to fully offset federal income taxes for workers at the poverty line. Under current law, a childless adult working full-time at the minimum wage is ineligible to receive any EITC benefits, but would receive the maximum credit if he or she had children. As a result, single childless adults are the only Americans that the federal income tax taxes into poverty. In the 2008 campaign, then-Senator Obama proposed a modest expansion of the EITC for childless workers, which was incorporated into the temporary Making Work Pay credit, but this provision is also scheduled to expire at the end of 2010.

“ The EITC rewards low-wage work by reducing the taxes that low-wage workers pay on their earnings and by supplementing their wages.”