



## Tax Credits for Low-Income Families: Questions and Answers

### 1. What do changes in tax laws have to do with ending hunger?

While ending hunger requires stronger nutrition programs, food assistance alone is not enough. Ending hunger also depends on increasing income for families who struggle to cover their household expenses. The tax system can help do just that. The Earned Income Tax Credit (EITC) is an efficient, proven, well-targeted way to add resources for low-income working families. With this credit, low-income families are better able to meet essential needs, including nutritious food and quality child care.

The poverty that causes hunger is largely due to a lack of money and resources. Food is one of the most flexible items in a low-income family's budget. Rent, transportation, child care, utilities—these are fixed expenses. As a result, food is often one of the first things cut when low-income families have to tighten their belts. Poverty forces drastic choices, like watering down a baby's formula to make it last longer. These tax changes would put more money in the pockets of low-income families, making it easier for them to make ends meet.

### 2. Why do low-income people get tax breaks like the EITC and I don't get similar credits or deductions on my taxes?

The tax code has many incentives that encourage taxpayers to make certain fiscal choices, like saving for retirement, attending college, or owning a home. But many of those tax credits are out of reach for low-income earners who often do not have the same tools for those kinds of expenditures or for long-term financial investments. Moreover, most tax deductions and exclusions are regressive, meaning they provide a larger benefit for wealthier individuals.

By expanding the benefits low-income workers receive, including making benefits refundable, tax credits encourage work and open up more financial choices. Programs like the EITC that benefit low-income working people represent only a fraction of the amount spent through the tax code. The EITC and Child Tax Credit (CTC) accounted for a little over \$111 billion, or about 10.3 percent, of the more than \$1 trillion spent through the tax code for all taxpayers in 2010.

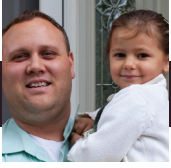
### 3. Many people pay no taxes at all in this country. Why is it fair for people like that to still have access to many government programs without helping to pay for them, and get a refund check from the government on top of that?

First, all Americans pay taxes. While some individuals do not pay income taxes, they still pay plenty in federal payroll taxes, sales tax, and other federal, state, and local taxes. Most of these other taxes are regressive, taking a larger share of a poor or middle-class family's income than wealthier families. In fact, most Americans pay more in payroll taxes than federal income taxes. The one-fifth of taxpayers with the lowest incomes pay 12.4 percent of their income in state and local taxes, which is significantly more than the rate that the top 1 percent of taxpayers pay, which is 8.4 percent. The EITC and CTC help offset this burden for many low-income working families.

The federal tax code includes provisions that reduce or eliminate tax liabilities for many individuals, at all income levels, and for corporations. But let's get back to the real question: shouldn't parents who work full time be able to support their families? The tax policies Bread supports help parents who work hard—who are trying to be responsible—achieve a basic standard of living and support their families. If Congress fails to continue the current CTC benefit levels, a single parent with two children working full time at minimum wage (earning about \$14,500 a year) will lose nearly \$1,500.

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### **4. Isn't this kind of refundable tax credit an example of income redistribution that forces hard-working citizens to pay for other people's poor decisions?**

Refundable tax credits enable low-income working parents to put food on the table and provide for their families, something working parents should be able to do no matter what economic conditions they live under. Yet, a parent with two kids working full-time at minimum wage in our country doesn't earn enough to keep the family above the poverty line. Refundable tax credits such as the EITC and CTC provide a boost in earnings so that full-time working parents don't have to raise their children in poverty.

These tax credits also promote economic mobility. A majority of EITC recipients only receive the credit for one or two years before moving on to higher income brackets. Moreover, they end up paying back more in taxes than they ever received in benefits.

### **5. These tax credits affect low-income people who are employed. What about the millions who are unemployed?**

Tax credits only provide benefits to people who have or recently had a job and therefore earned a taxable income. However, the EITC can provide a critical support to workers who, due to the recession and slow recovery, worked only part of the year or took a new job working fewer hours, or for a lower wage, and have become newly eligible for the program. Our nation's persistent economic downturn means that several issues need to be addressed right away, including the need for more and better jobs. Bread has chosen again to speak up so that low-income families can receive the most benefit for their work. This approach can put more money in the hands of poor families for years to come. Bread will also continue to advocate for extended unemployment benefits, boosts to job creation, and other supports to help those who may not immediately benefit from these tax credits.

### **6. Will "low-income" credits make people want to earn less money in order to qualify?**

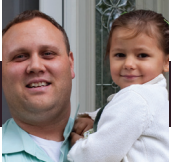
The EITC is structured so that for most people, the more wages they earn, the more benefits their families receive until they reach a set income threshold. When they reach the upper income limit, they see a decrease in their credit, not a complete loss. At its highest point, the EITC can provide a boost of 40 cents on the dollar. Yet, as wages increase and benefits decline, each additional tax credit dollar helps. This drastically reduces the potential for the EITC to act as a disincentive for higher earnings.

### **7. Without some restrictions on how to spend the benefits, how do we know that recipients will use the money wisely to help their families?**

While it's true that we can't control how people spend their tax benefits, the reality is that low-income families run out of money before they're able to address all of their needs. Research shows that about half of EITC benefits are used for long-term investments such as improving housing, transportation, or paying tuition. The other half is spent on purchases to meet immediate needs such as food, clothing, or catching up on rent and utilities. For all of us, our spending choices are limited by our available options. Bread for the World is looking to increase options for low-income families by increasing their resources.

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### 8. Don't the EITC and CTC have a lot of fraud and errors that waste taxpayer money?

Opponents of the EITC often criticize the program for having a high rate of overpayments. However, these error rates are often exaggerated and reflect the EITC's complexity more than actual fraud within the program. The tax code in general, and the EITC in particular, are confusing and difficult to calculate. For example, a non-custodial parent may be eligible to claim a child for the Child Tax Credit but not for purposes of the EITC.

Second, the EITC error rate is much smaller than the error rate in other parts of the code. A 2001 IRS study found that 51 percent of rent and royalty income, 57 percent of small business income, and 72 percent of farm income went unreported. The total cost to the federal government from misreporting business income (about \$109 billion) is at least 10 to 12 times the size of all EITC overpayments.

Finally, since the EITC works through income tax filings, it is self-administered and has much lower administrative costs than other direct spending programs. This puts money directly in the hands of working families rather than the government deciding where families must allocate their resources. Moreover, the infrastructure for these programs is already in place, and these expansions can provide low-income working families crucial relief without the inefficiencies caused by creating a new program.

### 9. Don't programs like EITC just create dependency on federal assistance?

Only people who are working can receive the EITC and CTC. They encourage work because the more money you make, the larger the credit you receive based on marital status and number of children. For example, a single parent with two children reaches the maximum credit amount once she earns \$12,570.

These policies encourage low-income working parents to work full time. Under current law, parents with two children who work just 10 hours a week at a minimum-wage job receive less than \$100 through the CTC, but if they work full time, they receive a credit of about \$1,800. This encourages people to work more, building on the basic value that work is better than welfare. According to the Committee for Economic Development, an organization comprised of 250 corporate executives and university presidents, "The EITC has become a powerful force in dramatically raising the employment of low-income women in recent years."

A majority of EITC filers receive the credit for only one or two years before moving into jobs with higher earnings. They end up paying back more in federal taxes than they received in benefits over their lifetimes. EITC participants generated nearly \$500 billion in net tax revenue between 1986 and 2006.

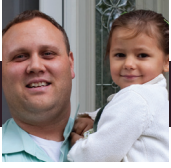
The EITC is the most effective anti-poverty program in the country, lifting more people out of poverty than any other program. In 2009, the EITC lifted an estimated 6.6 million people, including 3.3 million children, out of poverty. President Reagan called the EITC the "best anti-poverty measure" passed out of Congress.

### 10. Do the EITC and CTC reward low-income people for having large families?

No. Families with at least three children get a larger EITC than families with one or two children. However, families with four or more children do not see a larger benefit. Furthermore, if Congress lets the current benefit levels expire at the end of 2012, families with three or more children will no longer receive a larger credit even though their poverty rates are higher.

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There is no limit to the number of children a family can claim for the CTC. However, low-income families receive a smaller credit than higher-income families. A family must earn at least \$3,000 to be eligible. Upon reaching the \$3,000 mark, a low-income family can get 15 percent of every dollar earned above \$3,000. Because of how the credit is structured, the actual amount a family can receive as a refund check is capped, regardless of how many children a low-income family has. Thus, the CTC does not reward low-income people from having large families.

### **11. In tight budget times, why should wealthy people receive benefits under the CTC?**

The CTC benefits low-income, middle-income, and wealthier households. Families with incomes above \$110,000 generally see a phase down in their credit amount. Refundable tax credits are at risk, especially with calls in Congress to reform the tax code and eliminate many of the current credits and forms of “spending through the tax code.” The fact that middle-class families also claim the CTC gives this benefit wider support and less vulnerability to elimination, which would harm low-income families. However, in the current budget climate, the refundability of these credits remains at serious risk.

### **12. Everything on Capitol Hill is so partisan these days, especially anything relating to taxes. Won't these tax credit programs just create more partisan division in Congress?**

The EITC and CTC have a long history of bipartisan support. The EITC was enacted under President Ford and expanded under Presidents Reagan, Clinton, Bush, and Obama. President Reagan called the EITC the best anti-poverty measure of his administration. Conservatives like the EITC and CTC because they provide a clear incentive for people to work. Liberals like it because it is less bureaucratic than other anti-poverty programs, and it restores some fairness to the tax code. Nearly all funding goes directly to workers, rather than to pay for administrative costs. In an era of heightened partisanship, these tax credits are something everyone can support.

