The Earned Income Tax Credit and CalEITC

The Lifting Children and Families Out of Poverty Task Force
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Outline

I. What is the Federal EITC?
II. What does the research show about direct and longer run effects on child poverty
III. Opportunities for the Task Force recommendations: CalEITC
Federal Earned Income Tax Credit

• Largest anti-poverty program for children in the U.S.
• In 2015, almost 20 percent of all tax filers and 44 percent of filers with children receive the credit.
• Work contingent, requires positive earnings
Who receives the EITC?

<table>
<thead>
<tr>
<th>Demographic Group</th>
<th>% Dist. of Recipients</th>
<th>% Dist. of Expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single, with children</td>
<td>59%</td>
<td>74%</td>
</tr>
<tr>
<td>Married, with children</td>
<td>19%</td>
<td>23%</td>
</tr>
<tr>
<td>No Children</td>
<td>22%</td>
<td>3%</td>
</tr>
</tbody>
</table>

Distribution of earnings for select demographic groups (IRS SOI data)
(a) Single filers with 1 child
(b) Married couples with 1 child

Notes:
- Share (E<=0) = .03, Share (E>200K) = .003
- Share (E<=0) = .026, Share (E>200K) = .061
II. Direct effects of the EITC
Effects of the EITC on disposable income (→ poverty)

- The EITC affects after-tax-and-transfer income through:
  - Credit effect: direct EITC payments
  - Earnings effect: expected to increase employment due to conditioning on work
  - Income adjustment effect: offsetting reduction in public assistance (SNAP, TANF) as earnings increases
II. Direct effects of the EITC

- EITC leads to increases in employment for single parents (Eissa and Liebman QJE 1996, Hoynes and Patel 2016)
  - $1000 increase in EITC → 6–7 pp increase in employment
- Relatively small reduction in employment of secondary earners in low earnings families (Eissa and Hoynes 2004)
- Evidence of self employed workers reporting income to maximize the EITC credit (Saez 2010)
- Very efficient transfer – EITC leads to gains in after tax income due to credit amount and induced earnings: induced earnings accounts for half of the total anti-poverty effects (Hoynes and Patel 2016)
EITC raises incomes between 75% to 175% of FPL

The 1993 expansion led to a 7.9 percentage point increase in the share of single mother families with after tax and transfer above 100% poverty.

Static versus Dynamic Calculations of Anti-Poverty Effects

Simulated number of children raised above income-to-poverty cutoffs

Ignoring the behavioral response leads to an underestimate of the anti-poverty effects by 50 percent.

II. Effects of the EITC in the longer run
Effects of the EITC on health

• The EITC leads to a reduction in risky biomarkers in mothers and improvement in mental health (Evans and Garthwaite 2014).

• The EITC leads to a reductions in low birth weight births (Hoynes, Miller and Simon (2015)

• These are not long term outcomes *per se*, but serve as important markers of possible long run effects.
Effects of the EITC on human capital and education

- The EITC leads to increases in children’s reading and math test scores (Dahl and Lochner (2012), Chetty et al (2011))

- The EITC leads to increases in educational attainment and college going (Bastian and Michelmore (2015), Maxfield (2013) and Manoli and Turner (2014))
II. Effects of the EITC in the longer run

• **Bottom line:** additional income in childhood leads to better outcomes across the life course.

• **This is not a trade-off:** instead more direct effects today lead also to more indirect effects down the road.
Opportunities for the Task Force recommendations: CalEITC

- California introduced the CalEITC in 2016.
Typical State EITC Policies

- Most states have refundable tax credits, simple % of federal credit

- CALIFORNIA DID SOMETHING DIFFERENT

Source: Tax Policy Center.
The California EITC

Montialoux and Rothstein, IRLE Policy Brief, “The New California EITC”
FIGURE 2  Value of the California and federal credits for a single filer with two children,
FIGURE 3 Value of the combined California and federal EITC for single filers, 2015

Montialoux and Rothstein, IRLE Policy Brief, “The New California EITC”
The Income Limit to Qualify for the CalEITC Will Increase to $22,300 for Parents

Estimated CalEITC for Workers With Two Qualifying Children by Annual Earnings, Tax Year 2017

- **CalEITC Without the Expansion in 2017**
- **CalEITC With the Expansion in 2017**

**Expansion begins when annual income reaches $13,794 and CalEITC is $250.**

Annual income to qualify for CalEITC increases to $22,300.

Source: California Budget & Policy Center analysis of Section 17052 of the California Revenue and Taxation Code

Montialoux and Rothstein, IRLE Policy Brief, “The New California EITC”
CalEITC: Observations

• Resources targeted to lower earnings levels
• A large share of the CalEITC eligibles are not currently filing. Challenge for reaching the population (nationwide take-up is 80–85% but is lower for non-filers, those with low income levels)
• Uncertainty about the employment effects (compared to Federal); CalEITC only extended to those working at low earnings levels (e.g. minimum wage worker 20 hrs/wk x 52 wks/yr = $10,920, already close to phase-out point)
Opportunities for the Task Force: CalEITC

1. Expand the generosity of the CalEITC
2. Adopt the approach used by other states; simple percentage of Federal EITC
3. Encourage more take-home EITC (federal and state) by making not-for-profit tax preparation more accessible
4. Increase filing among CalEITC eligible (information treatments, text messaging)
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Project in development between CDSS CalFresh Division (Kim Wade), California Policy Lab, and Berkeley and Stanford researchers:

TREATMENT: Text messages to households informing them about the EITC, the amount of their potential benefit, and how to file their taxes online or at a local volunteer tax assistance site.

RCT: Structured to test efficacy of different treatments

DETAILS: The study will use CDSS’s records to identify select households in a handful of counties that the agency estimates are likely to be eligible for the EITC but unlikely to file their taxes.