

EITC Improves Fairness, Benefits to Working Families

Senate-Passed Bill Offers Local Economic Boost Across Iowa

By Charles Bruner and Andrew Cannon

The federal Earned Income Tax Credit (EITC) now represents the country's largest anti-poverty program, providing \$420 million in benefits in 2009 to over 200,000 Iowa households filing federal income tax returns, representing well over half a million Iowans.¹ A major purpose of the federal EITC is to promote work and enable low-wage working families with children to meet their families' basic needs. The federal EITC, as well as the child tax credit, is "refundable," so the families receive the benefit even if they do not otherwise owe any federal taxes, through a refund check.

Iowa has a state EITC that is calculated as a percentage (7 percent) of the federal credit, and it is also refundable. The Iowa Senate this session unanimously passed legislation to raise the state EITC to 13 percent for the 2012 tax year, going to 15 percent for 2013 and 20 percent for 2014. This would make Iowa's EITC more in line with Iowa's overall state income tax collections, which are about 30 percent the size of the federal income tax. Overall, according to a 2011 Iowa Department of Revenue report, 17 percent of all adults and 37 percent of all children in Iowa receive the state EITC.

Previous IFP Policy Briefs have described Iowa's EITC, its importance to working Iowa families, and the need to expand this credit to address what currently is the biggest inequity, or unfairness, in Iowa's tax system — its treatment of families with children. This Policy Brief examines the impact of raising the Iowa EITC from 7 percent of the federal EITC to 20 percent. First, it discusses how such a change would raise the threshold at which Iowa families start to owe state income taxes. Second, it provides information on how it would affect state and local economies, with information by current House legislative districts.

The Impact of Raising the EITC on Who Pays Iowa Income Tax

All Iowans pay taxes — through the sales tax, the property tax, and use taxes such as the gasoline tax. The state income tax is the only Iowa tax specifically based upon the ability to pay. Through personal credits, the standard deduction, and tax filing thresholds, a basic level of subsistence income is left untaxed. Iowa also has established specific exclusions for older tax filers. For instance, some pension income and most Social Security income are excluded from taxable income; over the next two years Social Security will become completely exempt from Iowa tax. As a consequence, retired individuals and couples with only Social Security and pension income do not begin to pay Iowa income taxes until they have much more income than working families do. The federal government also provides preferential treatment for Social Security income, but not nearly at the level Iowa does; in contrast, the federal government provides far greater recognition of the costs of raising children.

Table 1 shows how an increase in the state EITC would raise the state tax threshold (where families begin owing income tax) closer to the federal. The table also illustrates the much higher state thresholds for retirees, compared to working families, at every level of the Senate-passed state EITC. The federal poverty level for a family of four (two parents, two children) in 2011 was \$22,811; such a family pays some state income tax, as shown in Table 1. Raising the EITC from 7 percent to 20 percent would eliminate the state

Table 1. Higher EITC Allows Families to Earn More Before Owing State Income Tax

Family Type	State Tax Threshold 7 percent EITC	State Tax Threshold 20 percent EITC	Federal Tax Threshold
Single parent, 1 child	\$ 17,175	\$ 20,700	\$ 31,500
Married couple, 2 children (one income)	\$ 19,250	\$ 26,650	\$ 45,400
Married couple 2 Children (two incomes)	\$ 22,600	\$ 29,900	\$ 45,400
Retired individual SS/pension income only	\$ 41,100	—	\$ 31,000
Retired couple SS/pension income only	\$ 60,000	—	\$ 49,900

Note: Based on 2011 Federal tax law. Tax thresholds for working families were calculated assuming only wage income and a standard deduction. Married couples with equal incomes file separately and married couples with one income file jointly. For retired tax filers, the assumption is the individual has \$20,000 in Social Security and the rest in pension income and married couples have \$35,000 in Social Security and the rest in pension income.

income tax for working families with children below the federal poverty level. While Iowa’s tax system still would tax many low-income working families considered too strapped financially by the federal government to owe taxes, it would move toward greater fairness in overall taxation. Clearly, Iowa’s tax treatment of working families remains very different from its tax treatment of retired individuals and couples, even though costs for working parents raising children are generally greater than for taxpayers who receive retirement income.² Iowa is currently projected to provide over \$20 million in additional tax reductions to older Iowans (those above the current thresholds shown in Table 1) through its final phaseout of the tax on Social Security over the next two years.

Impact of Raising the EITC to 20 percent on Families and House Legislative Districts

In addition to having an impact upon tax filers, the EITC also has impacts upon local communities — as most families receiving the EITC use those funds to make necessary purchases at the community level. The benefits of the EITC are dispersed throughout the state, although they tend to be most prevalent in lower-income communities or communities with large proportions of families with young children. Table 2 provides information on the use of the federal EITC in 2009 by current Iowa Senate and Iowa House district. Table 3 estimates comparable size of the Iowa EITC at 7 percent vs. 20 percent of the federal level.

As Table 2 shows, all 100 House districts have over 1,000 households who receive the federal EITC and receive at least \$1.7 million in benefits. EITC benefits per district average \$4.2 million and reach a maximum of \$7.8 million. House districts with state universities and therefore high proportions of students, who generally do not qualify for the EITC, receive the least amount of benefits, while districts within high poverty urban neighborhoods generally receive the most. Raising the Iowa EITC from 7 percent to 20 percent would have an average benefit per House district of almost \$550,000, which residents would use in their local economy, with a high of slightly over \$1 million and a low of a little more than \$200,000.

¹ Iowa Department of Revenue, *Iowa’s Earned Income Tax Credit Tax Credits Program Evaluation Study*, revised February 2012, www.iowa.gov/tax/taxlaw/EITC2011_revised.pdf

² The greater need of families with children is evidenced in the 2011 Poverty Thresholds, calculated by the Census Bureau, which show that a single parent with one child needs at least \$15,504 per year to live above the poverty level, and a married couple with two children needs at least \$22,811, while an elderly couple needs \$13,596.

Charles Bruner is executive director of the Child & Family Policy Center (CFPC) in Des Moines, and **Andrew Cannon** is research associate at the Iowa Policy Project (IPP) in Iowa City. Together, CFPC and IPP are the Iowa Fiscal Partnership, a nonpartisan public policy research and analysis initiative. Reports are at www.iowafiscal.org.

Table 2. Iowans Filing for Federal EITC by Iowa Senate and House Districts — 2009

IA Dist.		Federal '09 Tax Returns			Fed. Val.	IA Dist.		Federal '09 Tax Returns			Fed. Val.
SD	HD	Returns	# EITC	% EITC	of EITC \$	SD	HD	Returns	# EITC	% EITC	of EITC \$
1	1	12,318	3,248	26%	7,372,159	26	51	13,172	1,834	14%	3,573,653
	2	11,609	3,140	27%	6,957,506		52	12,405	2,369	19%	5,013,693
2	3	12,828	1,739	14%	3,540,064	27	53	12,784	1,815	14%	3,516,733
	4	12,024	1,432	12%	2,822,968		54	13,345	2,319	17%	4,909,110
3	5	12,599	1,892	15%	3,754,336	28	55	12,360	2,171	18%	4,492,721
	6	13,806	2,016	15%	3,724,339		56	12,527	1,913	15%	3,738,044
4	7	11,722	1,950	17%	3,778,829	29	57	12,412	2,028	16%	3,944,814
	8	12,126	1,746	14%	3,560,342		58	12,063	1,928	16%	3,828,915
5	9	11,972	2,010	17%	4,085,118	30	59	16,182	1,498	9%	2,807,180
	10	13,140	1,575	12%	3,058,090		60	15,664	1,456	9%	2,643,137
6	11	12,251	1,922	16%	3,806,673	31	61	13,199	1,840	14%	3,446,799
	12	12,325	1,869	15%	3,694,110		62	12,362	2,873	23%	6,041,018
7	13	12,553	2,306	18%	4,331,103	32	63	16,827	1,397	8%	2,665,624
	14	12,407	1,901	15%	3,689,437		64	13,776	2,202	16%	4,503,305
8	15	12,747	1,982	16%	3,755,780	33	65	11,465	2,509	22%	5,381,911
	16	12,283	1,911	16%	3,682,345		66	11,266	3,262	29%	7,362,266
9	17	12,468	1,499	12%	2,941,562	34	67	15,918	3,042	19%	6,585,213
	18	12,151	1,969	16%	3,979,414		68	12,873	3,098	24%	6,746,745
10	19	11,901	1,141	10%	2,031,053	35	69	19,473	1,682	9%	3,186,690
	20	13,372	1,762	13%	3,375,674		70	20,028	1,579	8%	2,824,805
11	21	13,624	2,609	19%	5,248,447	36	71	12,703	1,579	12%	3,135,201
	22	12,240	3,499	29%	7,840,973		72	11,537	2,075	18%	4,330,719
12	23	12,266	1,697	14%	3,468,355	37	73	13,417	1,710	13%	3,418,887
	24	12,065	2,042	17%	3,934,575		74	14,366	1,762	12%	3,389,566
13	25	13,353	2,065	15%	4,137,000	38	75	12,387	2,020	16%	3,993,294
	26	12,261	2,589	21%	5,429,248		76	13,255	1,857	14%	3,688,171
14	27	12,270	2,281	19%	4,581,671	39	77	12,945	1,559	12%	2,473,783
	28	14,483	2,228	15%	4,264,548		78	13,071	1,585	12%	2,537,799
15	29	13,636	1,327	10%	2,428,000	40	79	13,182	1,842	14%	3,617,285
	30	19,138	2,304	12%	4,115,535		80	13,371	2,639	20%	5,302,252
16	31	13,496	1,879	14%	3,563,695	41	81	15,797	2,442	15%	5,052,735
	32	13,569	1,811	13%	3,502,897		82	14,527	1,471	10%	2,796,508
17	33	14,514	2,786	19%	5,508,996	42	83	13,913	1,732	12%	3,303,406
	34	14,041	2,193	16%	4,341,216		84	13,829	2,377	17%	5,204,469
18	35	14,642	1,593	11%	3,017,932	43	85	14,164	2,877	20%	6,482,734
	36	17,091	2,046	12%	3,816,465		86	12,133	3,211	26%	7,120,251
19	37	14,157	1,793	13%	3,425,518	44	87	11,795	2,097	18%	4,265,225
	38	12,980	1,954	15%	3,696,406		88	12,616	2,706	21%	5,774,778
20	39	13,297	1,716	13%	3,439,115	45	89	12,950	1,890	15%	3,775,391
	40	12,812	1,811	14%	3,763,619		90	12,029	2,420	20%	4,476,954
21	41	12,347	2,076	17%	3,865,072	46	91	11,843	1,993	17%	4,053,853
	42	15,880	2,108	13%	4,196,032		92	11,950	2,663	22%	5,592,687
22	43	12,265	2,502	20%	5,150,469	47	93	12,174	2,837	23%	5,582,878
	44	12,444	1,935	16%	3,957,210		94	11,399	2,350	21%	4,903,794
23	45	11,129	1,079	10%	1,678,418	48	95	12,171	2,503	21%	5,264,076
	46	13,913	1,424	10%	2,319,274		96	11,476	2,271	20%	4,797,818
24	47	18,583	1,659	9%	3,015,324	49	97	11,407	1,989	17%	3,875,632
	48	12,611	2,052	16%	4,157,126		98	13,084	1,662	13%	3,360,446
25	49	11,942	2,236	19%	4,715,279	50	99	13,532	2,380	18%	4,959,822
	50	11,414	1,925	17%	3,880,091		100	13,097	3,193	24%	6,979,877

Total Iowa Filers of 2009 U.S. Returns: 1,323,286
Total Iowa Filers Claiming U.S. EITC: 208,736 (16%)

Total Credited to Iowans: \$419,122,075

Source: Brookings Institution

Table 3. Approximate Impacts of Increasing Iowa EITC from 7 to 20 Percent of Federal Credit (Based on 2009 Returns)

IA Dist.		Fed. Val.	Iowa \$	Iowa \$	Increase	IA Dist.		Fed. Val.	Iowa \$	Iowa \$	Increase
SD	HD	of EITC \$	At 7%	At 20%		SD	HD	of EITC \$	At 7%	At 20%	
1	1	7,372,159	516,051	1,474,432	958,381	26	51	3,573,653	250,156	714,731	464,575
	2	6,957,506	487,025	1,391,501	904,476		52	5,013,693	350,959	1,002,739	651,780
2	3	3,540,064	247,804	708,013	460,208	27	53	3,516,733	246,171	703,347	457,175
	4	2,822,968	197,608	564,594	366,986		54	4,909,110	343,638	981,822	638,184
3	5	3,754,336	262,804	750,867	488,064	28	55	4,492,721	314,490	898,544	584,054
	6	3,724,339	260,704	744,868	484,164		56	3,738,044	261,663	747,609	485,946
4	7	3,778,829	264,518	755,766	491,248	29	57	3,944,814	276,137	788,963	512,826
	8	3,560,342	249,224	712,068	462,844		58	3,828,915	268,024	765,783	497,759
5	9	4,085,118	285,958	817,024	531,065	30	59	2,807,180	196,503	561,436	364,933
	10	3,058,090	214,066	611,618	397,552		60	2,643,137	185,020	528,627	343,608
6	11	3,806,673	266,467	761,335	494,867	31	61	3,446,799	241,276	689,360	448,084
	12	3,694,110	258,588	738,822	480,234		62	6,041,018	422,871	1,208,204	785,332
7	13	4,331,103	303,177	866,221	563,043	32	63	2,665,624	186,594	533,125	346,531
	14	3,689,437	258,261	737,887	479,627		64	4,503,305	315,231	900,661	585,430
8	15	3,755,780	262,905	751,156	488,251	33	65	5,381,911	376,734	1,076,382	699,648
	16	3,682,345	257,764	736,469	478,705		66	7,362,266	515,359	1,472,453	957,095
9	17	2,941,562	205,909	588,312	382,403	34	67	6,585,213	460,965	1,317,043	856,078
	18	3,979,414	278,559	795,883	517,324		68	6,746,745	472,272	1,349,349	877,077
10	19	2,031,053	142,174	406,211	264,037	35	69	3,186,690	223,068	637,338	414,270
	20	3,375,674	236,297	675,135	438,838		70	2,824,805	197,736	564,961	367,225
11	21	5,248,447	367,391	1,049,689	682,298	36	71	3,135,201	219,464	627,040	407,576
	22	7,840,973	548,868	1,568,195	1,019,326		72	4,330,719	303,150	866,144	562,993
12	23	3,468,355	242,785	693,671	450,886	37	73	3,418,887	239,322	683,777	444,455
	24	3,934,575	275,420	786,915	511,495		74	3,389,566	237,270	677,913	440,644
13	25	4,137,000	289,590	827,400	537,810	38	75	3,993,294	279,531	798,659	519,128
	26	5,429,248	380,047	1,085,850	705,802		76	3,688,171	258,172	737,634	479,462
14	27	4,581,671	320,717	916,334	595,617	39	77	2,473,783	173,165	494,757	321,592
	28	4,264,548	298,518	852,910	554,391		78	2,537,799	177,646	507,560	329,914
15	29	2,428,000	169,960	485,600	315,640	40	79	3,617,285	253,210	723,457	470,247
	30	4,115,535	288,087	823,107	535,020		80	5,302,252	371,158	1,060,450	689,293
16	31	3,563,695	249,459	712,739	463,280	41	81	5,052,735	353,691	1,010,547	656,856
	32	3,502,897	245,203	700,579	455,377		82	2,796,508	195,756	559,302	363,546
17	33	5,508,996	385,630	1,101,799	716,169	42	83	3,303,406	231,238	660,681	429,443
	34	4,341,216	303,885	868,243	564,358		84	5,204,469	364,313	1,040,894	676,581
18	35	3,017,932	211,255	603,586	392,331	43	85	6,482,734	453,791	1,296,547	842,755
	36	3,816,465	267,153	763,293	496,140		86	7,120,251	498,418	1,424,050	925,633
19	37	3,425,518	239,786	685,104	445,317	44	87	4,265,225	298,566	853,045	554,479
	38	3,696,406	258,748	739,281	480,533		88	5,774,778	404,234	1,154,956	750,721
20	39	3,439,115	240,738	687,823	447,085	45	89	3,775,391	264,277	755,078	490,801
	40	3,763,619	263,453	752,724	489,270		90	4,476,954	313,387	895,391	582,004
21	41	3,865,072	270,555	773,014	502,459	46	91	4,053,853	283,770	810,771	527,001
	42	4,196,032	293,722	839,206	545,484		92	5,592,687	391,488	1,118,537	727,049
22	43	5,150,469	360,533	1,030,094	669,561	47	93	5,582,878	390,801	1,116,576	725,774
	44	3,957,210	277,005	791,442	514,437		94	4,903,794	343,266	980,759	637,493
23	45	1,678,418	117,489	335,684	218,194	48	95	5,264,076	368,485	1,052,815	684,330
	46	2,319,274	162,349	463,855	301,506		96	4,797,818	335,847	959,564	623,716
24	47	3,015,324	211,073	603,065	391,992	49	97	3,875,632	271,294	775,126	503,832
	48	4,157,126	290,999	831,425	540,426		98	3,360,446	235,231	672,089	436,858
25	49	4,715,279	330,070	943,056	612,986	50	99	4,959,822	347,188	991,964	644,777
	50	3,880,091	271,606	776,018	504,412		100	6,979,877	488,591	1,395,975	907,384

Total U.S. Credits to lowans: \$419,122,075 — House Dist. Average: \$4,191,221 — Senate Dist. Average: \$8,382,442

Iowa Value at 7% (Current): \$29,338,545 — Iowa Value at 20% (SF2061): \$83,824,415.

Source: Brookings Institution