Strengthening Pathways to the Middle Class: The Role of Work Supports

*The Cost of Living in Iowa 2019 Edition, Supplement*

Peter S. Fisher and Natalie Veldhouse

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**Authors and Acknowledgments**

**Peter S. Fisher** is a national expert on public finance. Fisher holds a Ph.D. in Economics from the University of Wisconsin-Madison, and he is professor emeritus of Urban and Regional Planning at the University of Iowa. He is the author of numerous articles in refereed journals. His book *Grading Places: What Do the Business Climate Rankings Really Tell Us?* was published by Good Jobs First in 2013 and is now a website, Grading the States, at www.gradingstates.org.

**Natalie Veldhouse** is a Research Associate with the Iowa Policy Project. She previously conducted education and health policy research with the University of Iowa Public Policy Center. As a former AmeriCorps VISTA, Natalie coordinated research efforts for the Johnson County Hunger Task Force. She holds a Master of Social Work degree and a bachelor’s degree in Ethics and Public Policy from the University of Iowa.

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Preface

This report is a supplement to the seventh edition of *The Cost of Living in Iowa*, which focused on basic needs budgets for families in Iowa’s 99 counties and estimates of the proportion of families whose income falls below the basic needs level. This report focuses on work supports and how they affect basic family budgets.

As with the last report in 2018, we examine the major public supports available to low-income families in Iowa: Child Care Assistance, Food Assistance (SNAP), public health insurance for adults and children (Medicaid and hawk-i), premium assistance and cost-sharing for health insurance plans under the Affordable Care Act, the Low-Income Home Energy Assistance Program (LIHEAP), the federal and state Earned Income Tax Credits (EITC), and the federal and state child and dependent care tax credits (CDCC).

In this report we show how these programs help to close the gap between basic needs and the income received from work for many Iowa families, and the “cliff effects” that hinder the effectiveness of some programs. We also illustrate the impact of selected policy changes on families and their ability to meet basic needs.
Strengthening Pathways to the Middle Class: The Role of Work Supports


By Peter S. Fisher and Natalie Veldhouse

Introduction

Working full time, year round is not enough to guarantee a middle-class standard of living. About 1 in 5 working Iowa families, in fact, do not earn enough to meet basic needs. A number of things could be done to help such families move into the middle class. Policies are needed to improve both the demand side and the supply side of the labor market. On the demand side, we need more middle-class jobs with decent wages and benefits. On the supply side, we need more workers with the education and skills needed to qualify for most good-paying jobs.

Here we focus on a set of “work support” policies that help low-wage working families survive and keep their children out of poverty, and that provide a stepping stone to a better education and a better job. We lay out a set of policies to strengthen these pathways to the middle class:

- **Reform Iowa’s Child Care Assistance** (CCA) program to eliminate a huge disincentive called the cliff and to make CCA more effective as a help to parents trying to improve their skills and raise their wage level.
- **Expand the Earned Income Tax Credit** to provide even stronger support to low-wage workers, encourage more work effort, and keep children out of poverty.
- **Expand the Child and Dependent Care Tax Credit** to cushion the loss of Child Care Assistance.

These reforms should be combined with education policies that ensure future generations of Iowans receive a quality and affordable education, from preschool through post-secondary institutions. These policies would require:

- **Expansion of the universal preschool program**.
- **Support of K-12 education through adequate funding of state supplemental aid**, which has been held at about 1.8 percent per-pupil spending growth on average from FY2011-20, well below the increased costs of operating schools. More school funding would demonstrate a commitment to young people choosing whether to teach or go into another line of work.
- **Stronger efforts to make post-secondary education more affordable** by restraining tuition growth, inevitably requiring better state support of the community colleges and regents institutions.
Current Work Supports: An Overview

As we showed in the Cost of Living in Iowa Part 1, half the jobs in Iowa pay less than what single parent families need to meet a basic needs budget, and even childless couples and single individuals, as well as married couples with children, need well above the minimum wage. So how do those families get by? Some do without health insurance, and then risk medical indigency or bankruptcy. Some rely on friends or relatives for child care. Some simply do without. But many families get help closing the gap from one or more work support programs:

- Food assistance (the Supplemental Nutrition Assistance Program, or SNAP, formerly known as Food Stamps)
- The Low Income Home Energy Assistance Program (LIHEAP)
- Child Care Assistance (CCA)
- Public health insurance: Medicaid and hawk-i (Iowa’s child health insurance program)
- Subsidies for the purchase of health insurance through the Affordable Care Act (ACA)
- Tax credits: state and federal Earned Income Tax Credits (EITC), state and federal Child and Dependent Care Credits (CDCC), and the federal Additional Child Tax Credit.

Not included in this list is TANF (Temporary Assistance for Needy Families) because it does not really function as a work support: Any significant amount of earnings results in loss of eligibility. We also do not include public housing, because the coverage rate is so low (only about 25 percent of those income eligible actually receive public housing benefits) and waiting lists are so long, it does not really function as an effective support. We do not include the program to weatherize low-income homes for the same reason.

Figure 1 shows the maximum value of available work supports for a single parent with one child (age 3 to 5) at various hourly wages (assuming full-time work), starting at the current minimum wage. If we add the value of these work supports to the parent’s take-home earnings, the family’s total net resources (the height of the multi-colored column in the figure below) are still below

Figure 1. How Work Supports Decline as the Hourly Wage Rises

Single parent working full time, one preschool child

* Total family earnings, less: payroll and income taxes before refundable credits.
what the family needs to get by, as measured by the basic needs budget. This is the case until the hourly wage reaches $20, well above Iowa’s median wage of $17.84. The basic needs budget is the average cost of food, rent, transportation, child care, health care, and household expenses in Iowa, at a bare-bones level, with the cost of health care reflecting 2019 premiums for individual health insurance purchased on the Iowa exchange without subsidy.

It should be stressed that it would be unusual for a family to actually benefit from all available supports; the scenario above is the best possible. All these programs have participation rates (the percent of eligible families actually using the program) below 100 percent, and well below that for some, including one of the most important: Child Care Assistance. Benefits in some programs taper off as income increases: food assistance and the EITC are notable examples. This is clear in the shrinking value of these programs as the hourly wage increases. For the health care programs, adult Medicaid is partially replaced by ACA subsidies when the hourly wage reaches $11.25; those subsidies then taper off, while child Medicaid and then hawk-i benefits continue.

If we consider all work support programs except Child Care Assistance and the health insurance programs, the family’s total resources are always higher the higher the wage. It pays to get a better job, or to work more hours. (Program eligibility is based on total earnings, not the hourly wage, so working more and earning a higher wage have the same effect on eligibility.) The most striking effect, however, is the abrupt loss of the most valuable work support, CCA. For this family, CCA disappears at a wage of $11.80, at which point the family’s net resources — earnings plus program benefits — drop by about $4,600. The loss of adult Medicaid at a wage of $11.25 also creates a cliff, as the ACA subsidies at that point do not fully replace the value of Medicaid, leaving the family with about $3,100 more in health expenses. These “cliff effects” will be explored in more detail below. The combined effect of both the health care and child care cliffs when the wage rises from $11.20 to $11.80 is a drop in the family’s net resources of over $7,300.

Figure 2 shows that for a married couple with two children, both parents working full time, similar cliff effects leave the family with resources well below the basic needs level until the

Figure 2. Similar Cliff Effects Seen in Work Supports Available for Married Couple
Both work full time, two children (one age 4, one age 6-11)
hourly wage that each parent earns reaches $16.50. Food assistance and the EITC both disappear at a relatively low hourly wage. Adult Medicaid is replaced with ACA subsidies when the hourly wage reaches $8.55, resulting in a $6,100 reduction in net resources for the family. Child Care Assistance is lost when both parents earn more than $9.00 per hour, at which point the family loses another $8,200 in resources. The combined effect of both cliffs, when the hourly wage rises from $8.50 to $9.00, is a loss of resources equal to nearly $14,000.

A more realistic picture of the role of work supports in bridging the gap between earnings and the basic needs budget would take into account the actual utilization of each program. Of all the families who meet the eligibility requirements for a program, only some fraction will actually participate and receive benefits, for a variety of reasons — failure to comply with reporting requirements, lack of awareness of the program, a belief that one is not eligible, or a reluctance to receive public assistance. In the case of public housing there is simply insufficient funding for all who are eligible. For child care assistance, the parent may not be able to find a provider in the area who will accept the state’s reimbursement rate, which is well below the current market rate for many providers.

For most programs there are Iowa-specific participation estimates, though most are out-of-date:

- SNAP: 88 percent (2016)²
- EITC: 79.3 percent (2016)³
- Medicaid and haw-k-i: 89 percent (2013)⁴
- CCA: 32 percent (2001-2003)⁵
- LIHEAP: 38 percent (2004)⁶

Most work supports end well below income needed to meet basic needs because they are tied to outdated definitions of poverty, not to a realistic measure of a living wage. Figure 3 shows the relation between a basic-needs income needed to support families and the official poverty line.

**Figure 3. Official Poverty Level Is Well Below Income Needed to Meet Basic Needs**

Source: Authors’ analysis for The Cost of Living in Iowa, 2019 Edition
The family supporting income for families with children in Iowa ranges from 1.8 to 2.7 times the official federal poverty guideline (FPG) for their family size (considering households with all adults working). Yet eligibility for most work support programs is tied to a ratio of income to the poverty level and well below the family supporting level. As shown in Table 1, this ratio is below 1.7 for several important work supports, and reaches a ratio consistent with basic needs only in the case of hawk-i and ACA subsidies. This means that families must stop accessing essential work supports, such as assistance for food, utilities and child care, before they can meet their basic needs through employment alone.

Table 1. Most Programs Cut Off Eligibility Before Family Supporting Income Level is Reached

<table>
<thead>
<tr>
<th>Family Supporting Income: Ratio to FPG</th>
<th>Program Eligibility Ceiling: Ratio to FPG</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>EITC SNAP LIHEAP Medicaid (adults) Medicaid (children) hawk-i ACA Premium Subsidies* CCA CDCC</td>
</tr>
<tr>
<td>Young single living alone</td>
<td>2.16 1.22 1.30 1.75 1.38 NA NA 3.52 NA NA</td>
</tr>
<tr>
<td>Young married couple, no kids</td>
<td>2.61 1.24 1.30 1.75 1.38 NA NA 4.00 NA NA</td>
</tr>
<tr>
<td>Married couple, one child</td>
<td>2.71 2.22 1.30 1.75 1.38 1.67 3.02 4.00 1.45 2.29</td>
</tr>
<tr>
<td>Married couple, two children</td>
<td>2.53 2.06 1.30 1.75 1.38 1.67 3.02 4.00 1.45 1.86</td>
</tr>
<tr>
<td>Single parent, one child</td>
<td>2.40 2.44 1.30 1.75 1.38 1.67 3.02 4.00 1.45 2.97</td>
</tr>
<tr>
<td>Single parent, two children</td>
<td>2.19 2.21 1.30 1.75 1.38 1.67 3.02 4.00 1.45 2.30</td>
</tr>
</tbody>
</table>

Note: For all families, these figures are for the case where all adults work full time. The ratio of family supporting income to FPG (Federal Poverty Guidelines) ranges from a low that applies to a family with health insurance from the employer, to a high for a family purchasing health insurance on the private market. Eligibility ceilings for the EITC and for ACA premium subsidies were calculated from the authors’ cost of living policy model based on program rules. The program eligibility ceilings in all cases are not dependent on the work status of the parents, but the ratio of family supporting income to FPG is lower for married couples with only one working — 1.1 to 2.3 (not shown here).

*The eligibility ceilings for ACA subsidies are deceptive; for example, for a single parent with two children, annual benefits fall to zero at 250 percent of poverty (FPG); then when the children lose hawk-i benefits (at 302 percent FPG), the family is once again eligible for premium subsidies, but the amount falls to less than $500 annually at 350 percent of poverty before disappearing at 375 percent FPG.

Food assistance is a vital support for Iowa working families. SNAP benefits disappear at 130 percent of poverty, but play an important role in helping to fill the basic-needs gap for the lowest income households. As of September 2019, 315,473 Iowans in 152,271 households received food assistance. The average benefit per recipient was $110 per month, or $228 per household.⁷

Some programs, like the EITC, gradually reduce benefits as income increases, so when the eligibility ceiling is finally reached, there is no drastic loss of benefits. Other programs produce a cliff effect when income rises just above eligibility: the loss of benefits is substantial, creating a penalty for earning more. The figures below illustrate how the loss of benefits from various programs affects a family’s net resources: earnings after income taxes, plus benefits. When food assistance (SNAP) is lost, the two-earner couple with two children (Figure 4) experiences a reduction in resources of $828. But the loss of CCA eligibility pushes the family over an $8,292 cliff, while the loss of adult Medicaid costs the family over $6,000.⁸

Some programs gradually reduce benefits as income increases, so there is no drastic loss of benefits when eligibility expires.

But other programs produce a “cliff effect” — a two-earner family with two children is pushed over an $8,300 cliff when eligibility vanishes for Iowa’s child care assistance benefit.
Figure 4. Child Care Assistance Produces a Large Cliff Effect Compared to Other Benefit Programs

How net resources change as earnings increase for a two-earner couple with two children, ages 4 and 7

<table>
<thead>
<tr>
<th>Hourly Wage (each parent, full time)</th>
</tr>
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<tbody>
<tr>
<td>$7</td>
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<tr>
<td>---</td>
</tr>
<tr>
<td>$0</td>
</tr>
</tbody>
</table>

- **Basic Needs Budget:** $75,724
- **Net Resources**
- **SNAP**: 7.85
- **Adult Medicaid**: 8.55
- **CCA**: 9.00
- **LIHEAP**: 10.85
- **EITC**: 12.40

<table>
<thead>
<tr>
<th>Wage Level at which Benefit Disappears</th>
</tr>
</thead>
<tbody>
<tr>
<td>SNAP: $7.85</td>
</tr>
<tr>
<td>Adult Medicaid: $8.55</td>
</tr>
<tr>
<td>CCA: $9.00</td>
</tr>
<tr>
<td>LIHEAP: $10.85</td>
</tr>
<tr>
<td>EITC: $12.40</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Cliff (reduction in net resources)</th>
</tr>
</thead>
<tbody>
<tr>
<td>SNAP: $(528)</td>
</tr>
<tr>
<td>Adult Medicaid: $(6,169)</td>
</tr>
<tr>
<td>CCA: $(8,292)</td>
</tr>
<tr>
<td>LIHEAP: $(279)</td>
</tr>
<tr>
<td>EITC: None</td>
</tr>
<tr>
<td>hawk-i: $(2,937)</td>
</tr>
</tbody>
</table>

In Figure 5 the cliffs are shown for a single parent with one preschooler.

Figure 5. Child Care Assistance Produces a Large Cliff Effect Compared to Other Benefit Programs

How net resources change as earnings increase for a single parent with one preschool-age child

<table>
<thead>
<tr>
<th>Hourly Wage (full time)</th>
</tr>
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<tbody>
<tr>
<td>$9</td>
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<tr>
<td>---</td>
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<tr>
<td>$0</td>
</tr>
</tbody>
</table>

- **Basic Needs Budget:** $43,832
- **Net Resources**
- **SNAP**: $10.30
- **Adult Medicaid**: $11.25
- **CCA**: $11.80
- **LIHEAP**: $14.25
- **EITC**: $19.40

<table>
<thead>
<tr>
<th>Wage Level at which Benefit Disappears</th>
</tr>
</thead>
<tbody>
<tr>
<td>SNAP: $10.30</td>
</tr>
<tr>
<td>Adult Medicaid: $11.25</td>
</tr>
<tr>
<td>CCA: $11.80</td>
</tr>
<tr>
<td>LIHEAP: $14.25</td>
</tr>
<tr>
<td>EITC: $19.40</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Cliff (reduction in net resources)</th>
</tr>
</thead>
<tbody>
<tr>
<td>SNAP: $(806)</td>
</tr>
<tr>
<td>Adult Medicaid: $(3,106)</td>
</tr>
<tr>
<td>CCA: $(4,622)</td>
</tr>
<tr>
<td>LIHEAP: $(323)</td>
</tr>
<tr>
<td>EITC: None</td>
</tr>
<tr>
<td>hawk-i: $(1,578)</td>
</tr>
</tbody>
</table>
In that case, the cliffs are less pronounced because the benefits are scaled to a two-person family rather than a four-person family. Still, the loss of child care assistance produces far and away the largest cliff: $4,622. And for this family, even if they participate in all possible assistance programs, their net resources do not approach the basic needs budget amount even at the state median wage level. This family needs around $20.25, more than $2 per hour above the median wage.

Funding and eligibility for SNAP and LIHEAP are entirely federal. In the remainder of this report we focus on four work support programs where the state of Iowa plays a major role in determining eligibility and/or benefits: health insurance, child care assistance, the state Earned Income Tax Credit, and the state Child and Dependent Care Tax Credit.

**Medicaid, hawk-i, and the Affordable Care Act**

Iowa’s Medicaid expansion (called the Iowa Marketplace Choice Plan) took effect in January 2014. The expansion raised the eligibility ceiling for adults from 100 percent to 138 percent of poverty, in effect pushing the cliff effect — sudden loss of Medicaid benefits — to an income level 38 percent higher than before. For children, eligibility now extends to 167 percent of poverty. But when the children lose Medicaid eligibility, the hawk-i program immediately takes over with a similar level of benefits, and continues up to 302 percent of poverty.

The Affordable Care Act provides two kinds of assistance for those not eligible for Medicaid. Premium assistance pays a share of the cost of qualifying insurance plans, at the bronze level or higher, purchased on the private market (most often through the state’s health insurance exchange), and is available for families with income up to 400 percent of poverty. Cost sharing pays part of out-of-pocket expenses (co-pays and deductibles) for those with income below 250 percent of poverty, but requires the purchase of at least a silver plan.

For a married couple with two children (a preschooler, and one age 6-11), the parents lose adult Medicaid when family income reaches 138 percent of poverty, or $35,535 (the equivalent of each parent earning about $8.54 an hour). But instead of facing a benefit cliff in the form of a $15,741 sudden loss of health benefits, the parent can now purchase insurance on the private market with subsidies and faces an additional expense of only about $6,169, the ACA subsidies covering the remainder. **The ACA in effect reduces a significant program cliff by 59 percent (Figure 6).** Those ACA subsidies then taper off quite gradually. Then when the children lose eligibility for hawk-i, the ACA subsidies once again kick in, eliminating most of the cliff from the loss of hawk-i benefits. When household income reaches 400 percent of poverty (at an hourly wage of $24.76), eligibility ends for all subsidies, but at that point the family is better able to handle the $6,988 cliff.

The ACA benefits would pick up a larger share of the loss of Medicaid if they purchased the silver plan because they would qualify for cost sharing as well as premium assistance.
A single parent with one child loses Medicaid at an hourly wage of $11.25. The ACA then kicks in with subsidies of about $4,104 for the purchase of adult insurance, which offsets 56 percent of the loss of adult Medicaid benefits (Figure 7).

As with the married couple, ACA subsidies taper off, then return to cover most of the loss of hawk-i when wages reach 300 percent of poverty. All subsidies end for the single parent above a $32.50 wage, but at that point the full cost of health insurance is more readily managed (Figure 7).^9
The expansion of Medicaid has provided health insurance for thousands of Iowans and almost certainly has driven down the percentage of Iowans without insurance. Combined with premium subsidies under the Affordable Care Act, Iowa families no longer face the large Medicaid benefit cliffs that once acted as a significant disincentive to earning more.

**Child Care Assistance**

Iowa’s Child Care Assistance (CCA) program covers the cost of child care for working parents with incomes below 145 percent of poverty, with modest co-pays required for those with income between 100 percent and 145 percent. As the family budgets illustrate, child care costs are a major financial barrier for those who have children below the school age and who are working to support themselves. For low-wage workers, CCA can be the most significant work support available to them.

While wages have stagnated, child care costs have continued to rise. Between 2013 and 2018, the state average cost of care in a licensed child care center rose 4 percent, though the cost of care in a licensed home in Iowa went unchanged. Over that same period, the federal poverty guidelines, which determine eligibility for child care assistance, rose about 9 percent.

Many families who are income-eligible for CCA do not take advantage of the program. There are several reasons: Some may be able to rely on family members such as grandparents for child care, some may be unable to find a child care provider in the area who is willing to accept the state reimbursement rate, while others may simply not know that they are eligible for the program or are unwilling to accept public subsidies. While the state reimbursement rates are periodically raised (most recently in 2018), they remain well below the actual cost charged by many child care providers. Providers may not collect the difference from parents between the subsidy and their usual rate. Instead, they must either accept the child at the lower rate, or refuse subsidized children. Of the 5,261 child care programs in the state as of July 2019 (centers, preschools, registered and unregistered homes), 1,510 (about one-third) did not accept subsidized children.

**Iowa has one of the lowest eligibility ceilings in the country.** As of 2018, only 10 states cut off eligibility for CCA at an income level below 145 percent of poverty. In 29 states, the threshold was over 170 percent, including 20 states with a ceiling of 197 to 307 percent. In six additional states the rate exceeded 240 percent in some portions of the state. It is clear from the family basic needs budgets that Iowa eliminates child care assistance at an income well below what a family needs to get by, which is two to three times the poverty level.

The cliff effect in Iowa’s CCA program is severe. A parent deciding whether to find a job that pays more per hour or to work more hours per week could find herself facing a dilemma: The higher earnings could push her over the benefit cliff so that getting the better job would make her family worse off. However, an important reform, the “CCA Plus” program, took effect in July of 2016: A family already receiving CCA whose income then rises above the eligibility ceiling can now continue to receive CCA for another year. With CCA Plus, the cliff effect is postponed as long as the family’s income is under a much higher eligibility ceiling. For example, for a family of four, monthly family income must remain under $5,940 for CCA Plus, compared to $3,112 under the regular program. This gives the family some time to make adjustments. In some cases, the child will age out of child care within that year. For others, however, those adjustments will still be as much of a challenge.
The situation facing a single parent with one preschool child is illustrated in Figure 8. Here we show the best-case scenario: The family participates in every program for which it is eligible. All other work supports (except for Medicaid) gradually taper off, approaching zero as the family nears the level of resources needed to meet basic needs. But Child Care Assistance disappears completely when the hourly wage hits $11.80. The result is a sudden drop in family resources of $4,622. The family’s child care costs (after child care assistance and the child care credits) go from 5 percent of income to 26 percent.

Reform of the program

The red area in Figure 8 shows how that cliff could be eliminated. First, eligibility is raised, in this example, to 200 percent of poverty. Second, a substantially more aggressive co-pay schedule kicks in once family income exceeds the current ceiling at 145 percent of poverty. A family’s required co-pay is based on family income and the number of “units” of child care, where a unit is a half day. Under the existing schedule, the co-pay or fee per unit rises by 25 cents each time income increases to the next step in the schedule. With our more aggressive co-pay schedule, the fee bumps up 70 cents instead of 25, an amount that is sufficient to increase the co-pay and taper benefits nearly to zero before they disappear.

The single parent with one child must cover 17 percent of child care costs at 145 percent of poverty (an hourly wage of $11.80). Under our alternative schedule, this share gradually rises to 74 percent as the hourly wage increases from $11.85 to $16.25 per hour (just below 200 percent of poverty). At $16.30, CCA ends. Federal and state child and dependent care credits remain, however, leaving the family to cover 83 percent of costs. With these reforms in place, the family just above 145 percent of poverty now still pays a portion of child care expenses, but their share (after child care assistance and child care credits) amounts to just 4 percent of income, instead of 26 percent under existing law. This percent gradually rises until, at 200 percent of poverty (where CCA disappears), the family’s net child care costs consume 18 percent of income.

Figure 8. How the Child Care Assistance Cliff Could be Eliminated

*Single parent with one child: Effect of raising eligibility to 200 percent of poverty and adopting higher co-pays*
Moderating the cliff effect in the CCA program is an important policy reform to ensure that working families in Iowa do not face a severe disincentive to getting a better job or working more hours. Parents earning just a dollar over minimum wage should not be faced with the prospect of making their family substantially worse off by bettering their work situation. Figure 8 shows that raising eligibility and instituting a higher co-pay replaces the cliff with a gradually declining benefit and greatly reduces the disincentive effect.

A fiscal note from the Iowa Legislative Services Agency from November 2017 estimates that increasing the eligibility ceiling for Child Care Assistance to 200 percent of the federal poverty level would cost $29,307,300. The cost estimate depends on how the co-pays are modified, and how rapidly benefits taper off.

**Child and Dependent Care Credit**

At an hourly wage of $14.85, a single parent with two children currently loses all child care assistance in Iowa. However, the federal and state child and dependent care income tax credits make up for a small part of that loss. Federal law allows parents to deduct 20 to 35 percent of their out-of-pocket child care costs (after any child care assistance) from their taxes. Iowa allows a credit for Iowa income taxes that starts at 75 percent of the federal credit, and this percentage declines as income increases, and disappears when income exceeds $45,000. The total amount of the two credits for the case of the single parent with two children is $2,109 at the point where CCA is lost, and rises to a maximum of $2,304.

The credits do not eliminate the cliff effect. A single-parent family with two children that increases earnings from $14.85 per hour to just over that amount will go from having 93 percent of child care costs covered by child care assistance and the credits, to having just 25 percent of the costs covered, as shown in Figure 9. As income rises further, the federal and state credits increase to a maximum level of 28 percent of child care costs.

**Figure 9. Child and Dependent Care Credits Compensate Slightly for Loss of Child Care Assistance**

*Single Parent with Two Children age 6-11, Statewide Average*
**Earned Income Tax Credit**

The federal Earned Income Tax Credit (EITC) and its Iowa counterpart supplement the earnings of low-wage workers through the income tax. The federal credit is a fixed percentage of wages (and the percentage is higher the more children in the family) until earnings reach a certain level, at which point the credit begins to phase out. The gradual phase-out is shown in Figures 1 and 2; there is no cliff effect with the EITC as benefits eventually taper to zero. The state EITC is 15 percent of the federal credit. Both the federal and state credits are refundable; if the family owes no income tax, they will still receive the full value of the EITC as a refund.

Many Iowa families with children pay state income tax even though they owe no federal tax; this includes many families with income below the federal poverty level. The EITC allows low income Iowans to earn more before owing any state tax. It also helps to fill the gap between earnings and the after-tax income required to meet basic needs. **The federal and state earned income credits together lifted out of poverty more than 10 percent of all Iowa taxpayers in 2014.**

In 2014, about 206,000 Iowa households benefited from the EITC, totaling over $460 million in benefits to working Iowa families as well as increased spending in the counties where they reside.

The EITC has proven to be an effective and efficient way to help low-wage workers make ends meet, particularly parents with dependent children. Research has shown that the EITC increases the work effort of recipients significantly by raising the rewards from work and making it more feasible for families with children to pay child care and other expenses necessitated by work. Furthermore, the beneficial effects last beyond the time when families actually receive the credit which is only a year or two at a time for the majority of families. The research found that women's wages rose more in later years as a result of the EITC and they were less likely to rely on cash welfare assistance. Furthermore, **the children of EITC recipients were healthier as a result, had better school performance, and earned more as adults.** These latter findings are consistent with earlier research showing the lifetime benefits accruing to children who are lifted out of poverty.


3 Kaiser Family Foundation at http://kff.org/medicaid/state-indicator/medicaidchip-child-participation-rates/?currentTimeframe=0&sortModel=%7B%22%22%22Location%22%2C%22%22sort%22%2C%22asc%22%7D These estimates are prior to Medicaid expansions under ACA.


5 FY2004 State LIHEAP Household Reports.


7 The cliff amounts represent the reduction in the family’s net resources — earnings after payroll and income taxes, plus program benefits — resulting from a five cent increase in the hourly wage, equivalent to a $100 increase in annual income.

9 While premium subsidies are available for families earning up to 400 percent of poverty, for a single parent with two children the cost-sharing formula is such that the family’s expected contribution, which is 9.5 percent of income once income exceeds 300 percent of poverty, exceeds the cost of health insurance in Iowa, so no subsidy is provided.

10 Statewide average child care rates from Iowa Child Care Resource and Referral, State of Iowa Data Sheets for July 2013 and July 2018. https://iowaccrr.org/resources/files/Data/FY19/FY19%20State%20Iowa.pdf The percentage increases in rates for infants, toddlers, 2-year-olds, 3-year-olds, and 4- and 5-year-olds were averaged.

11 According to one estimate, only 32 percent of those eligible participated; see footnote 7.

12 Iowa’s monthly reimbursement rate for center care for a 4-year-old in 2018 was $595, which was $227 (28 percent) below the 75th percentile of current market rates for this type of care. Iowa’s monthly reimbursement rate for center care for a 1-year-old was $738, which was $225 (23 percent) below the 75th percentile of current market rates for this type of care. National Women’s Law Center, “State Child Care Assistance Policies: Iowa.” May 2019. https://nwlc.org/wp-content/uploads/2019/05/Iowa-childcare-subsidy2018.pdf


15 Letter from Iowa DHS to Kent Ohms Nov. 9, 2017, in response to a request for information regarding the child care assistance program.

16 The federal credit is non-refundable, and therefore has a limitation equal to tax liability. As income rises, the limit will rise (because tax liability rises) and the credit will rise, even though the credit before the limitation is the same. The Iowa credit is refundable, and is calculated as a percent of the federal credit before the limitation. The credit starts at 75 percent of the federal and the percentage declines as income rises.


20 Marr, Huang, and Sherman.