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November 4, 2002

THE DISTRICT EARNED INCOME TAX CREDIT: HELPING WORKING FAMILIES ESCAPE POVERTY

By Jason Lakin and Ed Lazere

In 2000, the District enacted an Earned Income Tax Credit to build on the strengths of the federal EITC, which provides tax relief and refunds to low-income workers, particularly those with children. In 2001, the DC EITC was expanded, and it now equals 25 percent of the federal credit. Some 15 other states, including Maryland, also have a state Earned Income Tax Credit.

The Earned Income Tax Credit is designed to boost the incomes of families and individuals that remain poor despite working, which serves several important purposes. Most importantly, the EITC helps reduce child poverty. Research shows that the EITC now lifts more children out of poverty than any other government program. Because it makes work pay better, the EITC also encourages low-income parents to work and thus promotes welfare reform efforts.

New data from the District's Office of Tax and Revenue indicate that the DC EITC, now in its second year of existence, is providing substantial support to many DC households.

- Some 38,600 families and individuals received the DC EITC in 2002. The DC EITC reached roughly one in six DC households.
- The maximum DC EITC benefit was \$1,000, with the average family receiving \$442. Overall, the EITC provided nearly \$17 million in tax relief and income support to low-income workers and their families in the District.
- The DC EITC supports families throughout the city, although it provides particularly substantial benefits to certain areas. For example, 40 percent of the DC EITC recipients live east of the Anacostia River.

Moreover, there are indications that the participation rate in the DC EITC — that is, the proportion of eligible families and individuals that receive it — is relatively high. This is illustrated by comparing the number of DC EITC recipients with the number of District residents that receive the *federal* EITC. Since only families that claim the federal EITC recipients can get the DC EITC, this comparison is a reasonable measure of participation in the DC EITC.

- Some 39,000 families and individuals received the DC EITC, compared with roughly 50,000 District residents that receive the *federal* EITC.

- This means that nearly 80 percent of District residents who claim the federal EITC also claim the DC EITC. This is similar to the participation rates other states experienced in the initial years of their state EITC.

The substantial participation in the DC EITC can be attributed in part to outreach efforts that have been conducted by the District government and by the DC EITC Campaign, a coalition of non-profit, business, labor, immigrant, and religious organizations. The outreach efforts have focused on raising awareness of the EITC, helping DC residents understand how to apply for both the federal and the DC EITCs, and encouraging families to seek free tax preparation assistance. (More information on the 2002 outreach efforts can be found on the DC Fiscal Policy Institute web site, www.dcfpi.org.)

At the same time, these findings suggest that continued outreach efforts could help increase participation in the EITC further.

- Nationally, it is estimated that between 15 percent and 25 percent of families eligible for the *federal* EITC do not claim it. District families that fail to receive the federal EITC also are not receiving the DC EITC.
- In other states that have adopted an EITC, receipt of the state credit has reached 90 percent or more of the receipt of the federal EITC, particularly after the state credit has been in existence for several years. This is somewhat higher than the current participation rate in the DC EITC.

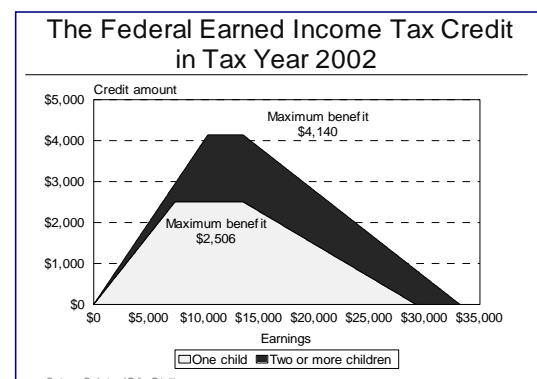
Thus, efforts to increase participation in both the federal and DC EITCs are warranted, and a goal of 90 percent participation in the DC EITC seems reasonable. If this participation rate were met, it would mean an additional 5,000 families and individuals would be receiving the DC EITC, and an additional \$2.2 million of tax relief and income support would be provided to DC's working poor families.

Both the DC government and the DC EITC Campaign are planning to engage in EITC outreach efforts in the 2003 tax filing season. These efforts are likely to broaden awareness of both the federal and the EITC and can be expected to contribute to an increase in the receipt of these credits among low- and moderate-income working residents.

The Importance of the EITC

The EITC is a tax credit for low- and moderate-income working families and individuals. The federal EITC is a *refundable* credit, which means that workers receive a refund check if the size of their EITC exceeds their tax bill. This is important because families with very low earnings often owe little or nothing in income taxes. Thus the EITC provides both tax relief and income support to low- and moderate-income workers.

Figure 1



For families with very low earnings, the value of the EITC *increases* as earnings rise. For families with two or more children, the federal EITC benefit for tax year 2002 equals 40 cents for each dollar earned up to \$10,350 of earnings, yielding a maximum benefit of \$4,140. The EITC benefit begins to phase out when income reaches around \$14,000, and eligibility for some EITC benefit remains until income reaches roughly \$33,000. For families caring for one child EITC, the maximum EITC is \$2,506, and eligibility phases out when income reaches about \$29,000. For wage-earners who are not raising children in their home, the EITC is far less generous. The maximum benefit is \$376, and the credit phases out completely when income reaches \$11,000.¹

The *DC EITC* is set at 25 percent of the federal EITC. A family that qualifies for a \$2,000 federal EITC, for example, is eligible to claim a \$500 DC EITC when they file their District income tax return. Like the federal credit, the DC EITC is refundable. The maximum DC EITC benefit is \$1,035 for a family with two or more children, \$627 for a family with one child, and \$94 for workers with no children.

The federal and District EITCs serve several important functions:

- *Reduce DC's high child poverty rate.* According to the 2000 Census, 31 percent of DC children are poor. Yet over half of the District's poor children live in families with one or more working adults. The EITC provides critical income support to families that work but remain poor. Research indicates that the federal EITC lifts nearly five million people out of poverty nationally, more than any other program.²

The DC EITC builds on the federal EITC to provide further income support to working poor families. For example, a parent with three children and full-time work at \$7.50 per hour would have net income of \$14,000 after federal payroll tax and DC income tax, or far below the \$18,104 poverty line for a family of four. This family would qualify for a federal EITC of \$3,702 and a DC EITC of \$925, which would bring its total income to \$18,627, or slightly above poverty.

- *Complement welfare reform.* In the District as in the nation as a whole, most parents leaving welfare for work have low wages and their families remain near or below poverty. The EITC provides support to families that move from welfare

Table I
EITC Benefits in 2002 For Families
With Two or More Children

	Federal	DC
	EITC	EITC
\$5,000	\$2,000	\$500
\$10,000	4,000	\$1,000
\$15,000	3,828	957
\$20,000	2,775	694
\$25,000	1,722	431
\$30,000	669	167

¹ Recent federal law changes increased EITC benefits modestly for some married-couple families. The figures cited here refer to benefits for single-parent families.

² See Center on Budget and Policy Priorities, "Strengths of the Safety Net: How the EITC, Social Security, and Other Government Programs Affect Poverty," 1998. (<http://www.cbpp.org/snd98-rep.htm>)

to low wage work. Research also has shown that the EITC encourages low-income parents to enter the labor market.³

- *Reduce high income taxes for near-poor working families in DC.* Without the DC EITC, a two-parent family with two children and income of \$20,000 would owe \$689 in DC income taxes, or more than in any other state except Kentucky. Such a family qualifies for a \$694 DC EITC, however, which fully eliminates its tax liability and provides a small \$5 refund. Including the EITC, the DC income tax liability at this income level is lower than in 19 states, and it is about the same as in 12 states that levy little or no income tax at this income level. The DC EITC reduces DC's income tax on near-poor families to a level that is in the middle when compared with other states.

Finally, it is worth noting that the federal and DC EITCs often help families meet critical needs or develop assets. Surveys indicate that common uses of EITC refunds include building savings, paying for education, purchasing or repairing a car, or obtaining better housing.⁴ Thus the EITC increases economic opportunities and economic security for low-income workers.

The DC EITC Helped Thousands of Low-Income DC Workers in 2002

In 2002, about 39,000 families and individuals — or nearly one in six DC households — claimed and received the DC Earned Income Tax Credit when they filed their 2001 tax return.⁵ The average benefit was \$442, and the total amount provided was almost \$17 million.

Table II and Figure 2 provide information on the number of DC EITC recipients by zip code. They show that there is a substantial number of EITC recipients in every ward except Ward 3.

Table II
DC EITC Recipients in 2002

Zip Code	Ward	DC EITC Recipients	Total Funds Claimed
20019	7	6,138	\$2,896,000
20020	7,8	5,734	2,756,000
20011	4,5	4,523	1,834,000
20002	5,6	4,339	1,928,000
20032	8	4,269	2,057,000
20001	1,2,5,6	2,771	1,184,000
20010	1,4	2,756	1,121,000
20009	1,2	2,558	1,037,000
20018	5	1,132	500,000
20003	6	1,120	480,000
20017	5	844	332,000
20024	6	692	300,000
20012	4	489	183,000
20005	2	376	138,000
Others		850	193,000
Total		38,591	\$16,939,000

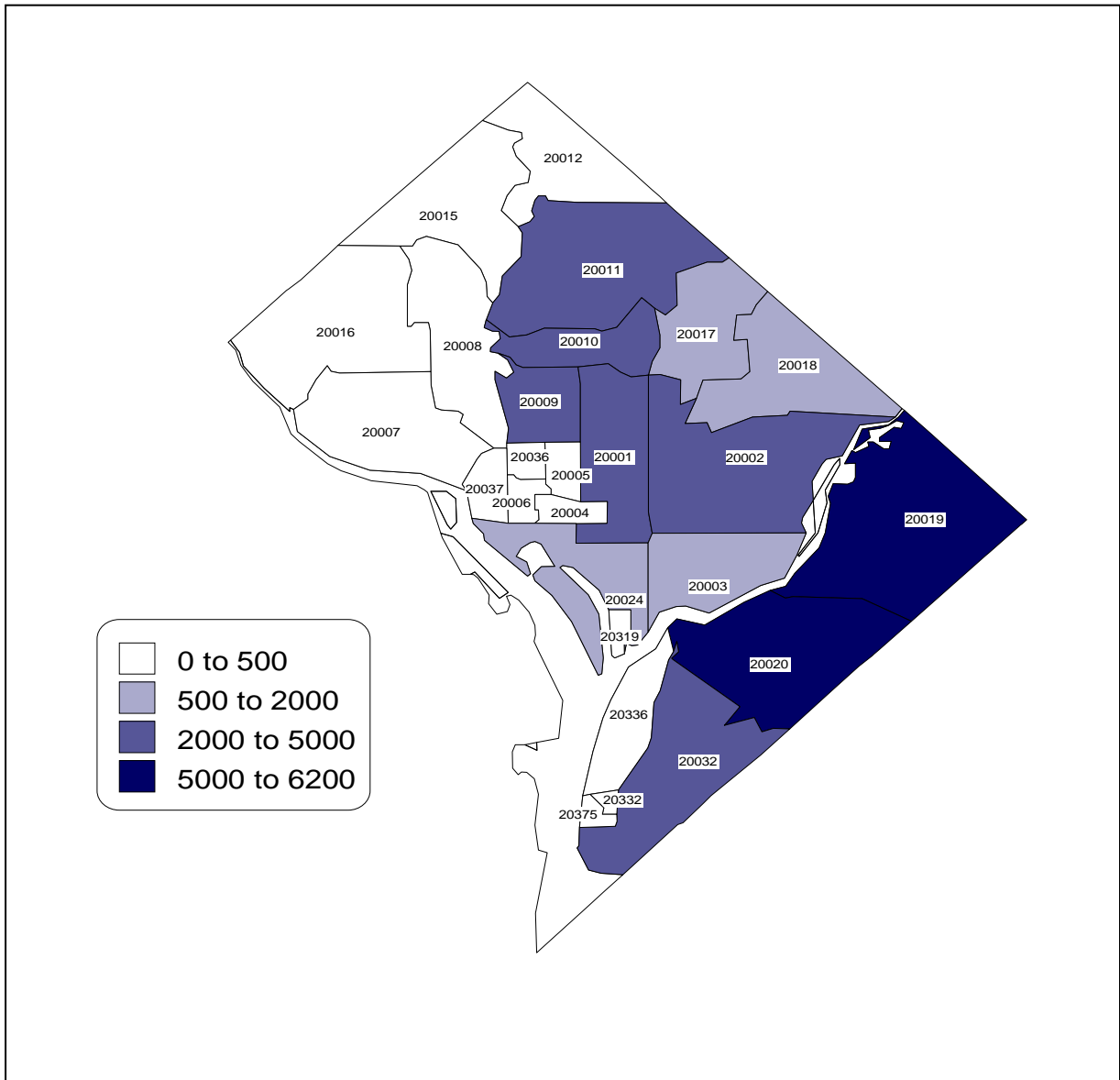
Source: DC Office of Tax and Revenue

³ See Center on Budget and Policy Priorities, "A Hand Up: How State Earned Income Tax Credits Help Working Families Escape Poverty in 2001," 2001, p. 10 (<http://www.cbpp.org/12-27-01sfp.pdf>).

⁴ Timothy M. Smeeding, Katherine E. Ross, and Michael O'Connor, "The EITC: Expectation, Knowledge, Use, and Economic and Social Mobility," *National Tax Journal*, December 2000.

⁵ Roughly 250,000 households live in the District. It should be noted that some households could include two or more EITC recipients. This could occur if two or more families or individuals within a household filed separate income tax returns. As a result, the number of DC households with an EITC recipient is likely to be modestly lower than 38,600.

Figure 2
2002 DC EITC Recipients by Zip Code



- About 40 percent of DC EITC recipients — 16,000 — live east of the Anacostia River in the 20019, 20020, and 20032 zip codes. Families in these areas received nearly \$8 million in tax relief and income support.
- Some 4,500 EITC recipients live in the 20011 zip code, in the lower portion of Ward 4 and the upper portion of Ward 5. An additional 700 EITC recipients live in the 20012 zip code, the other major zip code for Ward 4. Some 2000 EITC recipients live in the 20017 and 20018 zip codes in Ward 5.

- The 20002 zip code is the fifth largest in terms of EITC recipients, with 5,100 households receiving the credit. This zip code covers Ward 5 and Ward 6.
- Four other zip codes in the central portion of the city — 20001, 20003, 20009, and 20010 — include more than 9,000 EITC recipients. These zip codes are primarily in Wards 1, 2, and 6.

Participation in the EITC is Substantial

There are no precise estimates of the number of families and individuals who are eligible for the DC EITC. Available information suggests that a substantial share of the DC residents who are eligible for the DC EITC received it in 2002.

- Roughly 50,000 families and individuals in the District receive the *federal* EITC. While no local estimates exist, national estimates indicate that roughly 75 percent to 85 percent of EITC-eligible families claim it.
- Some 38,600 families and individuals claimed the DC EITC in 2002. This means that nearly 80 percent of the 50,000 DC residents who claim the federal EITC also claim the DC EITC. This participation rate is similar to the participation rates in other states in the initial years of their state EITC. In New York, for example, participation in the state EITC in its first year equaled 83 percent of federal EITC participation.⁶

Because the EITC is administered through the tax code, significant outreach efforts are needed to ensure that eligible families are aware of the credit and know how to claim it when they file a tax return. Throughout the nation, substantial outreach efforts are conducted by federal, state, and local governments, as well as by non-profit organizations, businesses, and community groups.

In the District, outreach efforts have been conducted primarily by the DC Office of Tax and Revenue and by the DC EITC Campaign, a coalition of non-profit, business, community, labor, immigrant, and religious organizations. The outreach activities included the distribution of fliers and brochures in several languages and the use of the District's social services hotline, *Answers, Please!*, as an EITC hotline. Information on the EITC was distributed through the DC Public Schools, and the DC Department of Human Services promoted the EITC through mailings to clients of several programs for low-income residents. In addition to raising awareness of the EITC, the DC EITC Campaign outreach materials also encouraged residents to take advantage of free tax preparation assistance and identified the sites where such assistance could be obtained.

The fact that nearly 40,000 District families and individuals claimed the DC EITC in 2002, only the second year of the credit's existence, suggests that the outreach efforts have been successful.

⁶ Center on Budget and Policy Priorities, "A Hand Up," op. cit, p. 29.

The Importance of Continued Outreach

At the same time, these findings suggest that continued efforts to increase participation in the DC EITC are warranted. As noted, it is likely that some DC residents fail to claim the *federal* EITC. These families also fail to receive the DC EITC. Moreover, roughly 10,000 District families and individuals claim the federal EITC but do not get the DC EITC.

In other states with state-level EITCs, participation in the state-level EITC typically reaches 90 percent or more of the participation in the federal EITC after the state-level credit has been in effect for several years.⁷ This participation rate seems like a reasonable goal for the District as well. If participation in the DC EITC were to rise to 90 percent of federal EITC participation, it would mean an additional 5,000 families and individuals would be receiving the DC EITC, and an additional \$2.2 million of tax relief and income support would be provided to DC's working poor families.

Because both the DC government and the DC EITC Campaign engage in EITC outreach efforts, it is likely that awareness of both the federal and the EITC will grow in and that the number of low- and moderate-income working residents receiving the EITC will increase.

⁷ Center on Budget and Policy Priorities, "A Hand Up," op. cit, p. 29.