



Earned Income Tax Credit (EITC)

What is the EITC?

The EITC is a refundable tax credit for working individuals and families who by and large earn less than 200 percent of the Federal Poverty Level (FPL) each year.¹ The EITC is intended to reduce the tax burden for low-income workers and supplement their wages. It has been part of the federal tax system since 1975 and has been expanded several times over the years. The EITC is one of the most successful federal anti-poverty programs. A report by the Center on Budget and Policy Priorities found that the federal credit now lifts more children out of poverty than any other government program. Approximately 4.8 million people, including 2.6 million children, are removed from poverty as a result of the federal EITC.

The EITC encourages work and can provide substantial income support for many low-income families. A single parent earning between \$10,350 and \$13,520 in 2002 and raising two or more children is eligible for the maximum EITC of \$4,140. Taxpayers with one child can claim a maximum EITC of \$2,506 and taxpayers who are childless can receive a tax credit of up to \$375.

Who is Eligible for the EITC?

In order to qualify for the EITC, a full-time, year-round worker with two children could not earn more than about \$15 an hour, however, most workers that claim the EITC earn less. To qualify for the federal EITC in tax year 2002, both earned and Adjusted Gross Income (AGI) must be less than:

Eligibility Requirements for the Federal EITC in 2003		
Number of Qualifying Children	Individual Filer	Joint Filer
None	\$11,490	\$12,490
One	\$30,338	\$31,338
Two or More	\$34,458	\$35,458
Source: Internal Revenue Service		

Participation

Nationally, 15.1 percent, or more than one in seven, of all tax filers claimed the federal EITC. In 2002, the EITC provided more than \$34 billion in benefits to 18.6 million working families in the United States. In Indiana, 398,515 tax filers claimed the federal EITC in 2002. However, between 15 to 20 percent of tax filers who qualified for the EITC did not claim the credit. According to the Internal Revenue Service, approximately \$8 billion went unclaimed nationwide in tax year 2000. In Indiana, 84,158 eligible Hoosiers did not claim the credit and lost out on approximately \$53 million in tax credits in 2001.

Despite this fact, the number of EITC claimants still rose by 1.5 million nationwide (8.5 percent) between tax year 2000 and 2002. The economic downturn and long-term employment trends, including layoffs, hiring freezes, decrease in wages, and reduced work hours, have contributed to this increase. Although Indiana's unemployment increases have been equivalent to the national average and have grown slowly over time, the number of people claiming the EITC rose 13 percent during the same time period.

Indiana State EITC

Indiana is one of seventeen states that offer a state EITC based on the federal EITC. In other words, taxpayers who are eligible for the Federal EITC are also eligible for the State EITC. Indiana's state EITC is refundable and claimants receive 6 percent of the federal EITC amount. The state EITC reaches working families with incomes up to \$32,000 a year and tax filers can receive as much as \$252. In 2002, Hoosier families who participated in TANF were refunded \$16.3 million in state EITC funds. Although the program has benefited many working Hoosier families, the credit is set to expire on December 31, 2005. If the tax credit expires many families will lose these much needed benefits, so it is vital that the state tax credit be renewed by the 2005 Indiana General Assembly.

Recommendations: Ways to Improve the State EITC

- 1. Expand the State EITC and make it a permanent part of the Indiana tax code.** The Indiana State EITC is set at 6 percent of the federal EITC but could be expanded to a larger percentage of the federal EITC. In addition, the state EITC is set to sunset (i.e., expire) on December 31, 2005. Indiana must make the state EITC a permanent part of tax code. Recently Illinois made their state EITC a permanent part of their tax code in May 2003 which will expand this benefit to nearly 200,000 additional working families.
- 2. Connect more families with the tax credits they have earned.** In early 2003, Governor Frank O'Bannon and the Indiana Family and Social Services Administration conducted an EITC promotion blitz which included media events, visits to newspaper editorial boards, letters to legislators and employers, and envelope inserts for TANF recipients, child care providers, and Section 8 landlords and tenants. However, more needs to be done including an education campaign to the public and social service providers and agencies that provide services to low-wage workers. Education and outreach materials should be in written and oral form should

be made available at workforce One-Stop Centers and include free and paid media in the following formats: Ads on television, radio, and in newspapers, Posters, Fliers, Grocery store bags, Inserts in utility, unemployment, or government assistance checks, and Indiana Congressional federal and state representatives newsletters.

- 3. Help families keep as much of their refunds as possible by supporting volunteer tax preparation programs.** Most people who get the EITC need assistance understanding the tax code and filing their forms. Unfortunately, the fees they pay for tax preparation and “fast cash” refund loans cost them hundreds of dollars and erode the effectiveness of the credit. Nationwide in 1999, an estimated \$1.75 billion EITC dollars were lost to tax preparation, electronic filing and high-cost refund loans. The state needs to take a leadership role and encourage communities to provide free tax preparation services to low-income and elderly residents that may be eligible for the EITC. There are two volunteer tax preparation programs known as Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE).

Sources:

Annie E. Casey Foundation KIDS COUNT Data
Brookings Center in Urban and Metropolitan Policy,
The Brookings Institute
Center on Budget and Policy Priorities

Finance Project
Indiana Family and Social Service Administration
Internal Revenue Service
Indiana Youth Institute
National Tax Assistance for Working Families Campaign

ⁱ In 2004, 200% of poverty is an annual income of \$31,340 for a family of three, and \$37,700 for a family of four.