

EITC and South Carolina

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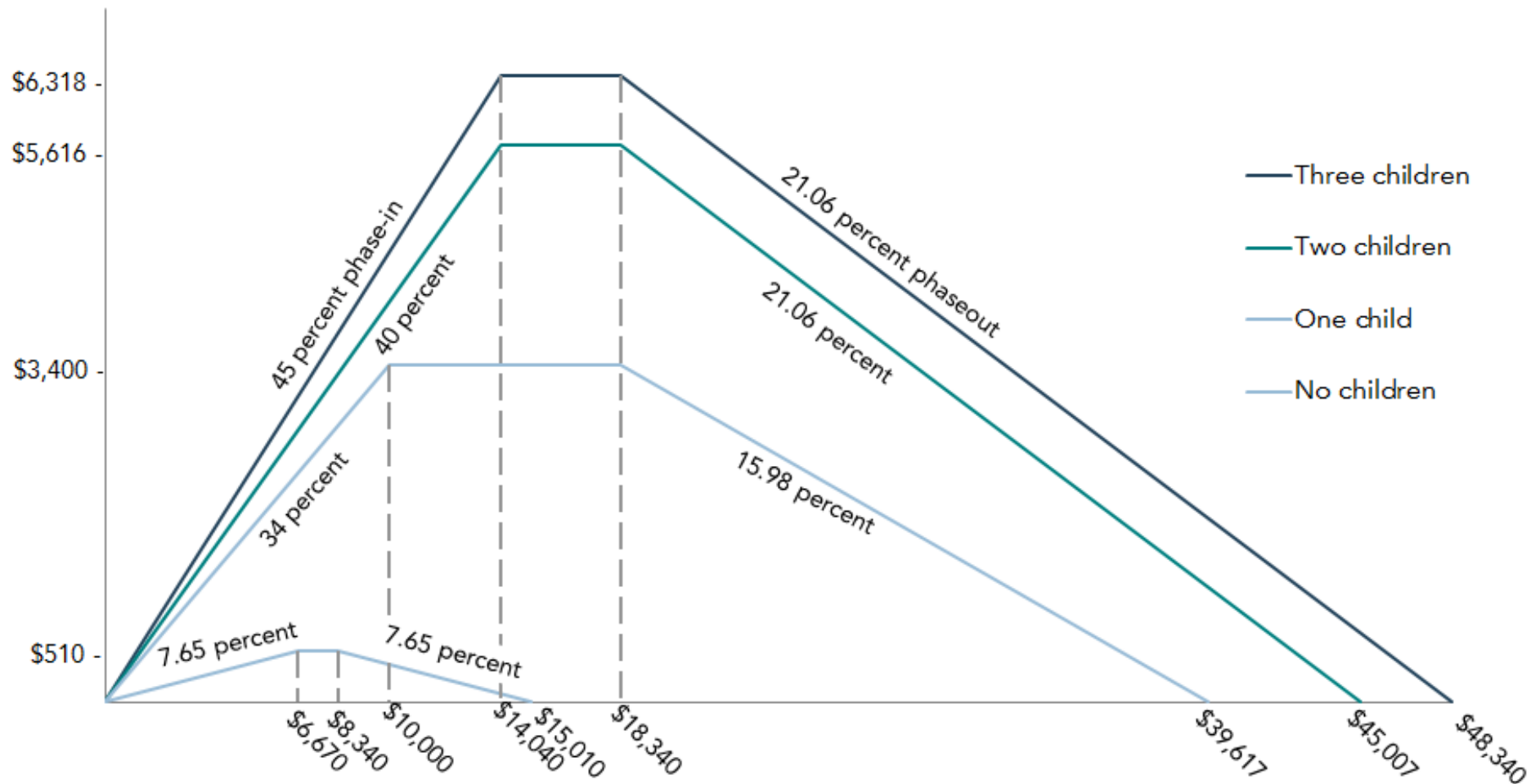
**REVIEW:
EARNED INCOMETAX CREDIT
(EITC)**



FIGURE 1
Earned Income Tax Credit
 2017



Credit amount



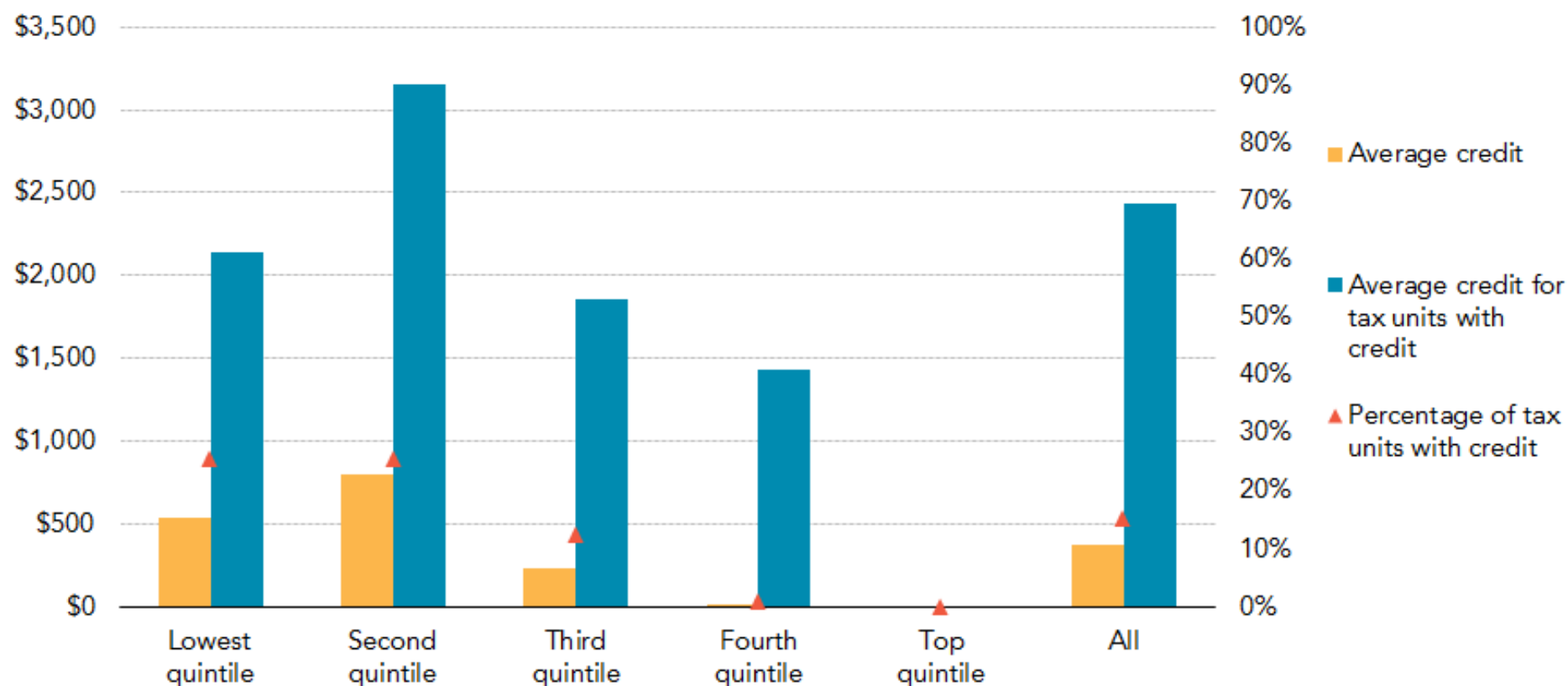
Source: Urban-Brookings Tax Policy Center; IRS Rev. Proc. 2016-55.

Note: Assumes all income comes from earnings. Amounts are for taxpayers filing a single or head-of-household tax return. For married couples filing a joint tax return, the credit begins to phase out at income \$5,590 higher than shown.



FIGURE 2

Distribution of and Percentage of Tax Units with EITC 2016

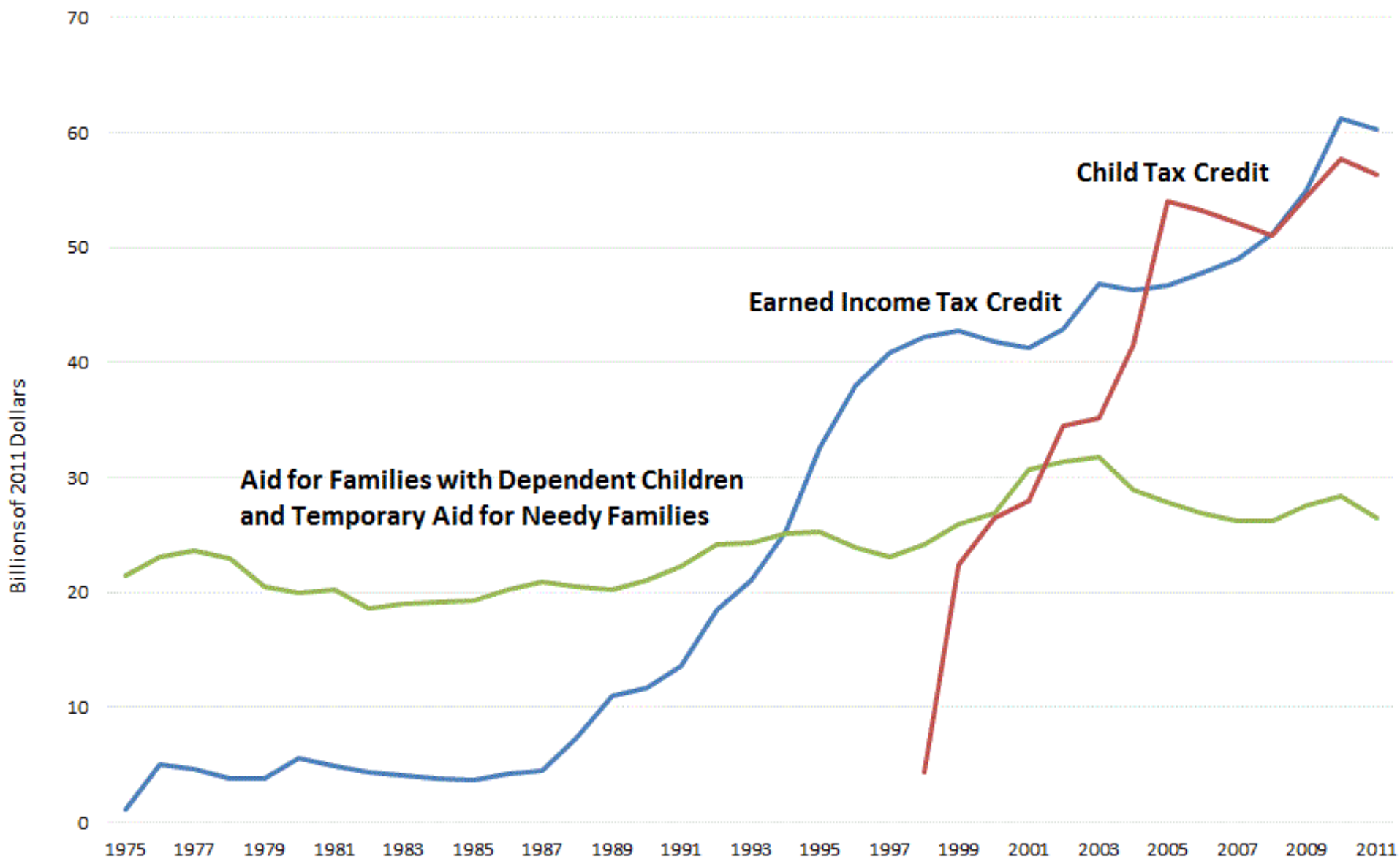


Source: Urban-Brookings Tax Policy Center Microsimulation Model, (version 0516-1).

Growth in EITC over time

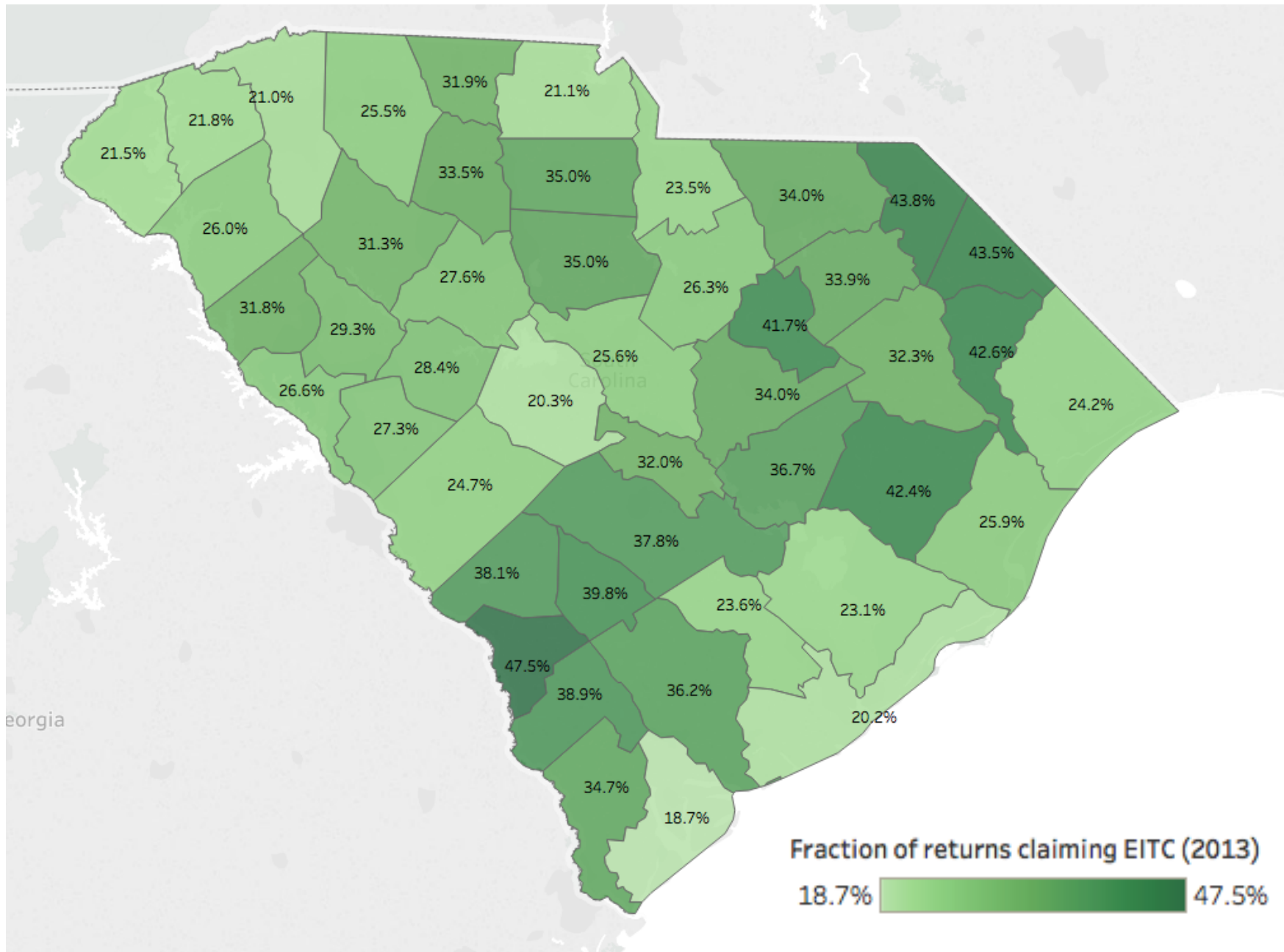
- 1975: The EITC was first made available and offered up to \$400 to low-income workers with children.
- 1978: The credit was made permanent
- 1986: credit was increased and finally indexed for inflation
- 1990: created a larger EITC for families with two or more children
- 1993: Increased the maximum EITC payment and created a small credit for families with no children
- 2001: raised the income level at which the EITC begins to phase out for couples to \$3,000 above that for single filers
- 2009: once again raise the income level for married couples and enacted a higher EITC rate for families with at least three children (through 2017)

Real Federal Spending on EITC, CTC and Welfare: FY1975-2011

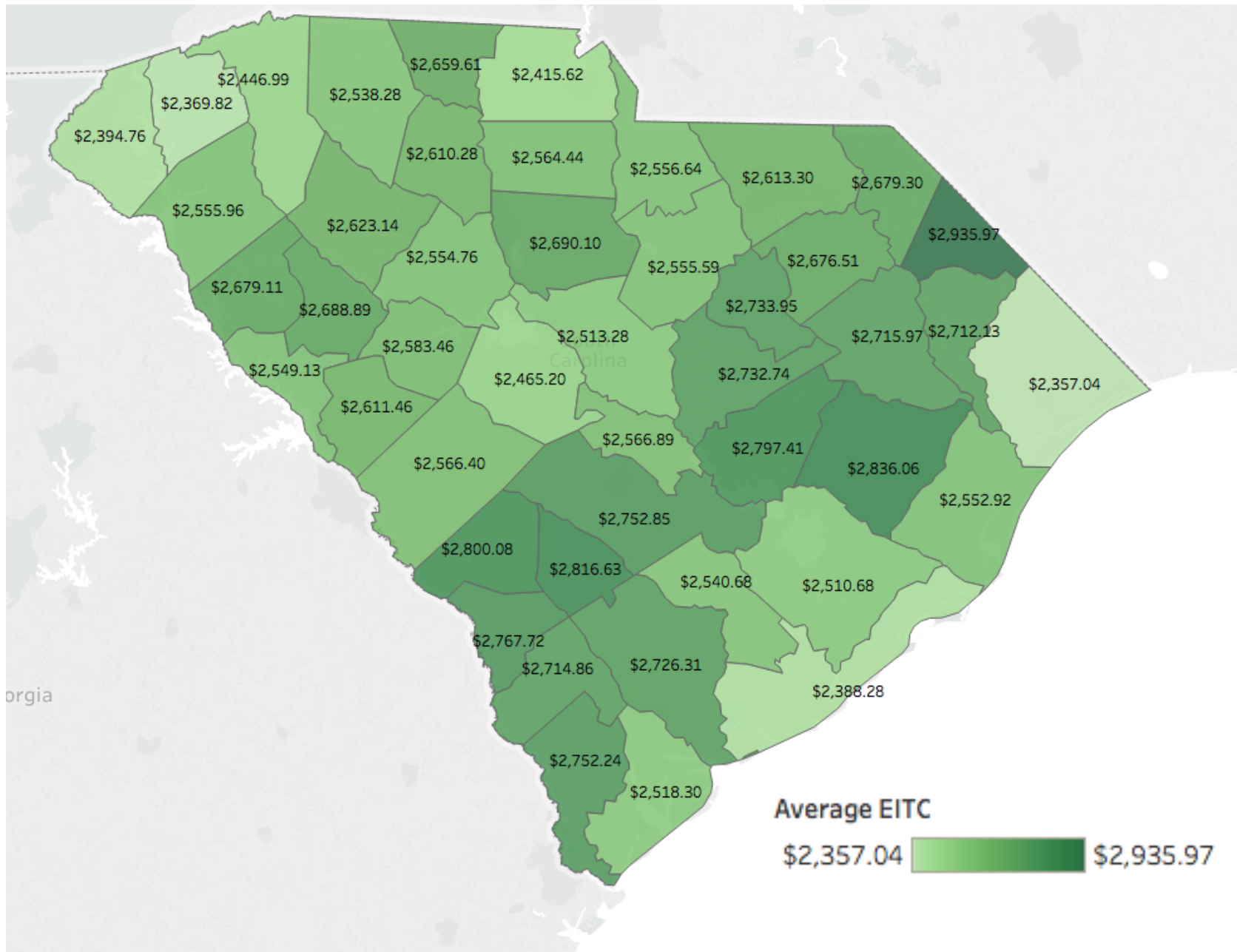


Sources: AFDC/TANF, SNAP: Budget of the United States Government, Fiscal Year 2014; for AFDC/TANF, "Family and Other Support Assistance" line; EITC and CTC: Internal Revenue Service Statistics of Income, various years; CPI deflator: Bureau of Labor Statistics. For CTC and EITC, we convert tax year data to fiscal year data by applying a 20-80 split.

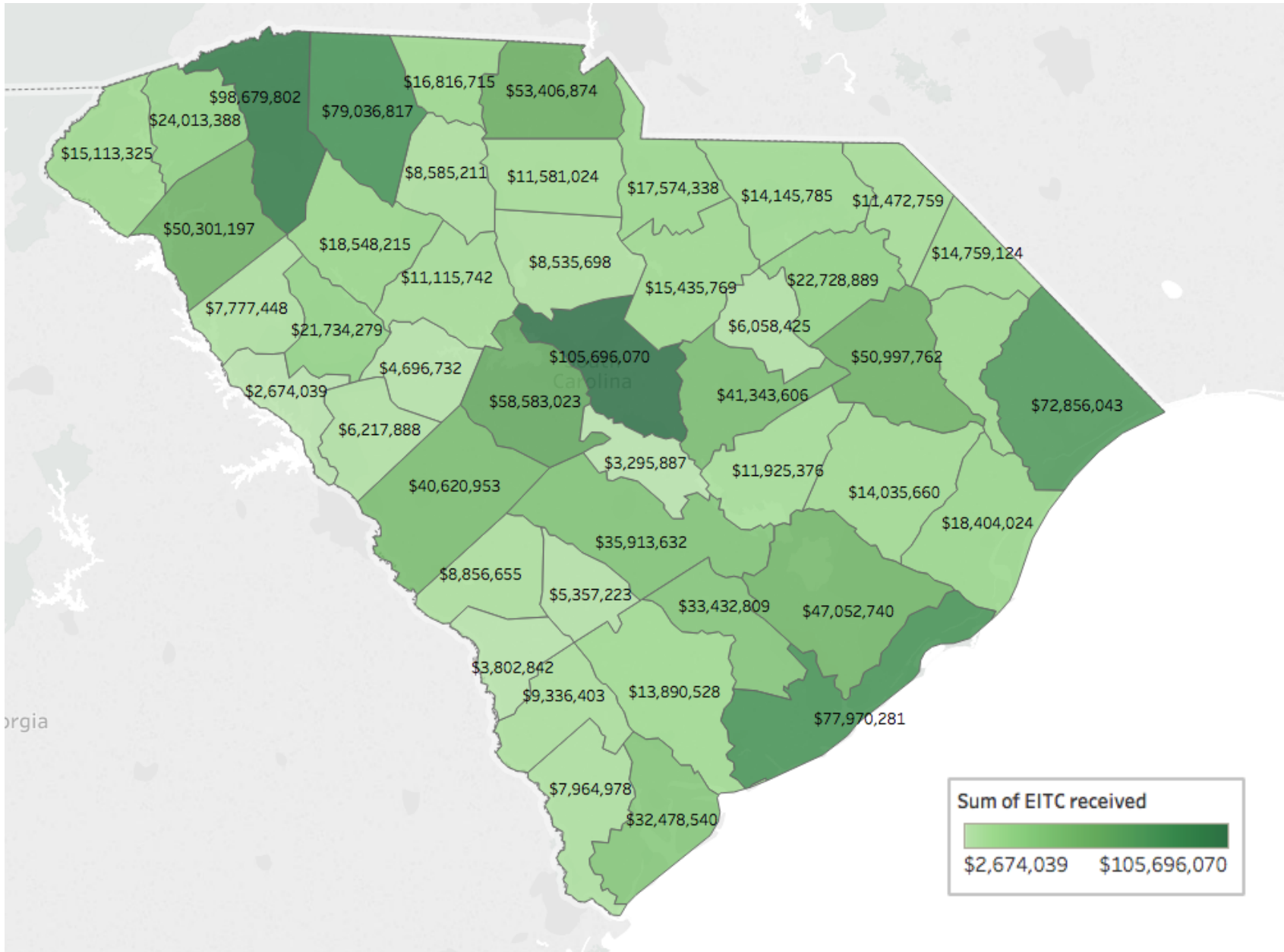
Percent of tax returns claiming EITC



Average EITC Claim



Total EITC Claimed



Impact of EITC – Labor Supply

- Labor Supply
 - Income effect: earn more income, work less
 - Substitution effect: work is more valuable: work more
- Evidence
 - Labor force participation
 - Increases for single mothers (Meyer and Rosenbaum 2001, Eissa and Liebman 1996)
 - Single mothers wind up experiencing long term income growth; they were not just taking dead end jobs (Dahl et al, 2009)
 - Slight decrease for married women (Eissa and Hoynes 2004)
 - Hours of work: no effect
 - EITC expansion in 1990s moved an estimated 500,000 families from cash welfare assistance to work (Dickert 1995)

Impact of EITC - family

- Health
 - Improved mental health for mothers with a high school degree or lower who had two or more children. Also, increased probability of mothers reporting excellent or very good health status overall. (Evans and Garthwaite, 2014)
 - Increased EITC income reduces the incidence of low birth weight and increases mean birth weight. For single mothers with 12 years of education or less, an increase of \$1000 in EITC was associated with a 7% reduction in low birth weight rate. (Hoynes et al, 2012).
- Education
 - \$1,000 increase in income raises combined math and reading test scores by 6 percent of a standard deviation. These effects are 2-3 times as large for children of non-white, unmarried, and less educated mothers. (Dahl and Lochner, 2012).
 - \$1,000 increase in tax credits raises students' test scores by 6% of a standard deviation leading to an increased probability of college attendance, higher earnings, reduction in teen birth rates, and improving the quality of neighborhood the kids live as adults. The results suggest that a substantial fraction of the cost of tax credits may be offset by earnings gains in the long run. (Chetty et al, 2011)
- Long term outcomes on kids
 - \$3000 increase in household income as a child is associated with 19% higher earnings as an adult and 135 hour increase in adult work hours (Duncan et al, 2010)

Impact of EITC – Poverty

- Brookings Institution analysis of Supplemental Poverty Measure Public Use Data
 - EITC kept 6.3 million (3.2 mil children) out of poverty in 2012
 - In SC, 96,000 (56,000 children)
 - In 2013, overall, lowered poverty rate by 2.9 percentage points....lowered child poverty rate by 6.4 percentage points
- Neumark and Wascher (2001) show that state EITCs increase transition out of poverty
- Gunderson and Ziliak (2004) suggest that the expansions in the federal Earned Income Tax Credit of the 1990s accounts for upwards of 50 percent of the reduction in after-tax income deprivation
- EITC contributed as much to decline in receipt of cash welfare among female headed families as did time limits and other welfare forms (Grogger, 2003)
- Many EITC recipients claim the credit for short periods and mostly to offset the temporary costs of a child's birth or spouses' loss of income. (Dowd and Horowitz, 2011)
- Uses of EITC are divided into those that improve economic and social mobility (car, tuition, move) and those that primarily help make ends meet (bills, food). (Smeeding et al 2000).

Multiplier Effect

- Refundable federal tax credit
 - Often constitutes largest payment households receive all year
 - Marginal propensity to consume is high
 - Significant spending on kids, durable goods (appliances), housing, and transportation (Romich and Weisner 2000)
- As summarized by Noble (2012), every \$1 of EITC realized generates economic activity of
 - \$1.07 in Nashville
 - \$1.40 in Fresno
 - \$1.58 in San Antonio
 - \$1.67 in Michigan

STATE EITC



Structure

- Model off of federal EITC
 - Shown to be successful
 - Lowers administrative burden
- Three dimensions on which it can vary:
 - % of federal
 - Refundable or not
 - Eligible family structures



TABLE 1

State Earned Income Tax Credits, 2016

State	Percentage of Federal Credit	Refundable?
California	85% of federal credit, up to 50% of the federal phase-in range	Yes
Colorado	10%	Yes
Connecticut	27.5%	Yes
Delaware	20%	No
District of Columbia ^a	40%/100%	Yes
Illinois	10%	Yes
Indiana ^b	9%	Yes
Iowa	15%	Yes
Kansas	17%	Yes
Louisiana	3.5%	Yes
Maine	5%	Yes
Maryland ^c	26%	Yes
Massachusetts	23%	Yes
Michigan	6%	Yes
Minnesota ^d	Avg. 34%	Yes
Nebraska	10%	Yes
New Jersey	35%	Yes
New Mexico	10%	Yes
New York	30%	Yes
Ohio ^e	5%	No
Oklahoma	5%	No
Oregon ^f	8%/11%	Yes
Rhode Island	15%	Yes
Vermont	32%	Yes
Virginia	20%	No
Washington ^g	10% (when implemented)	Yes
Wisconsin	4%- one child 11%- two children 34% - three children No credit- childless workers	Yes

^a The District of Columbia now offers a credit equal to 100 percent of the federal EITC to adults without dependent children with incomes up to twice the poverty line (for an individual).

^b Indiana decoupled from federal provisions expanding the EITC for families with three or more children and raising the income phase-out for married couples.

^c Maryland's refundable EITC will reach 28 percent of the federal credit by tax year 2018. The state also offers a non-refundable EITC set at 50 percent of the federal credit. Taxpayers in effect may claim either the refundable credit or the non-refundable credit, but not both.

^d Minnesota's credit for families with children, unlike the other credits shown in this table, is structured as a percentage of income rather than a percentage of the federal credit. It does not include the federal EITC's features of a larger credit for families with three or more children or higher income phase-out for married couples. The average given here reflects total projected state spending for the Working Family Credit divided by projected federal spending on the EITC in Minnesota as modeled by Minnesota's House Research Department; this average fluctuates from year to year.

^e Ohio's EITC is non-refundable and limited to half of income taxes owed on income above \$20,000.

^f Oregon's EITC is set to expire at the end of tax year 2019. In 2016, lawmakers increased the credit for workers with children 3 years and younger to 11 percent of the federal credit.

^g Washington's EITC has never been implemented, but would likely be worth 10 percent of the federal credit or \$50, whichever is greater.

Impact of State EITC?

- Effect on poverty
 - Cannot observe the effect of state EITCs on poverty
 - The Supplemental Poverty Measure only measures the federal EITC not any state EITCs
- Multiplier effect
 - Local spending increases
 - Job creation
 - Berube (2006) cites one new permanent job for every \$37,000 increased in EITC realization

SOUTH CAROLINA EITC



South Carolina EITC

- Part of H. 3516, the South Carolina Infrastructure and Economic Development Reform Act (Roads bill)
- Passed in May 2017

Earned income tax credit

- SECTION 16. A. Article 25, Chapter 6, Title 12 of the 1976 Code is amended by adding:
- "Section 12-6-3632. There is allowed as a **nonrefundable** credit against the tax imposed pursuant to Section 12-6-510 on a full-year resident individual taxpayer an amount equal to **one hundred twenty-five percent** of the federal earned income tax credit (EITC) allowed the taxpayer pursuant to Internal Revenue Code Section 32."
- B. Notwithstanding Section 12-6-3632, as added by this SECTION, the percentage of the federal earned income tax credit, for which the credit allowed by Section 12-6-3632 is based, must be **phased-in in six equal installments of twenty and eighty-three hundredths percent** each tax year until it is fully phased-in in tax year 2023, with the twenty and eighty-three hundredths percent applying in tax year 2018.
- C. This SECTION takes effect upon approval by the Governor and applies to tax years beginning after 2017.

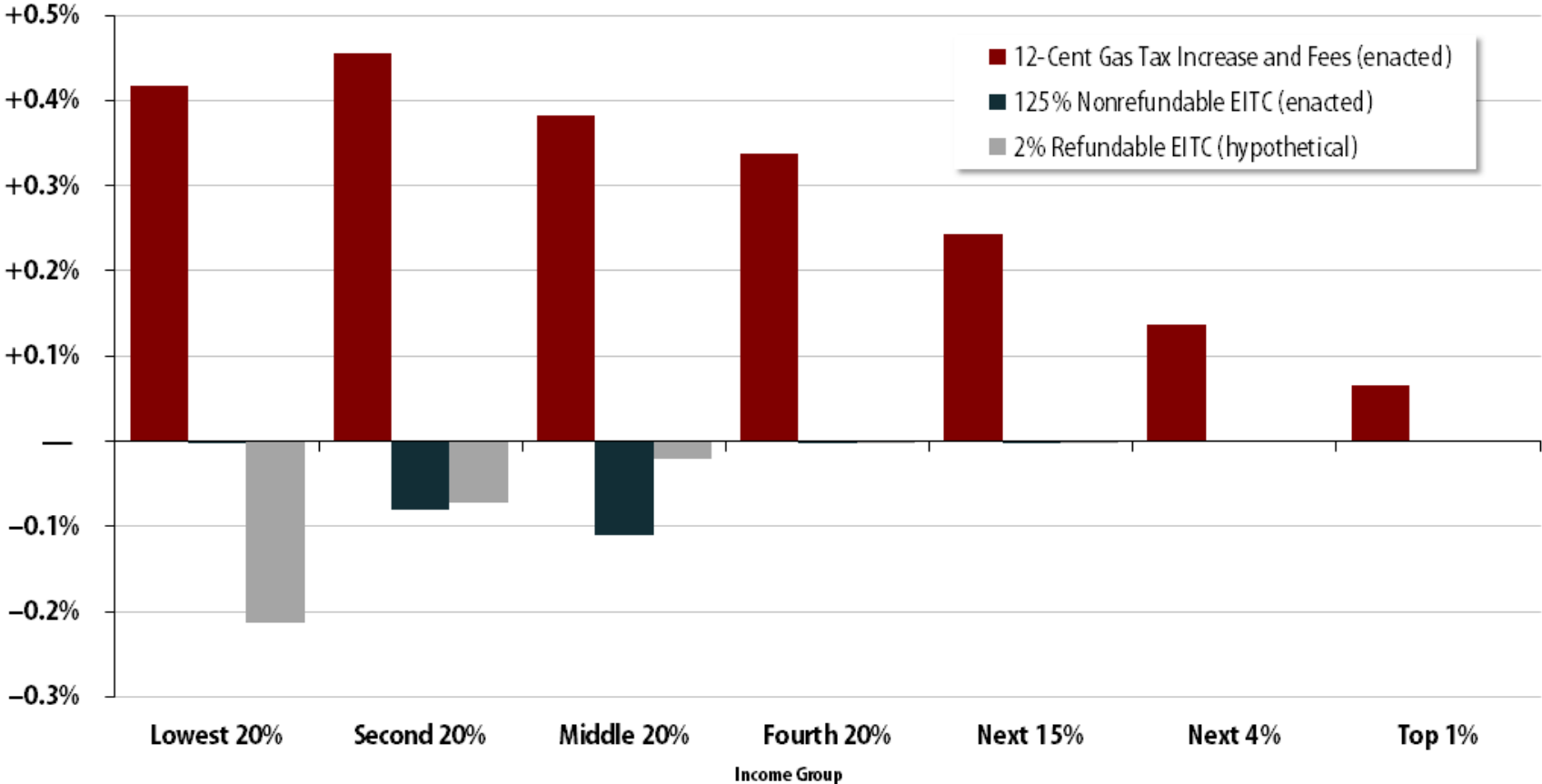
Who benefits from State EITC?

- Filers who claim federal EITC and who owe taxes to the State of South Carolina
 - 5.7% of total South Carolina filers
 - 23.5% of filers claiming the federal EITC
- Average federal credit received in South Carolina = \$2,545
- Average SC EITC (nonrefundable, 125% of federal) = \$286
- Total SC EITC in 2023: \$42,716,538
 - Including potential multiplier effect: \$45,706,695
 - Potential jobs created: 1,154

Refundable vs Nonrefundable EITC: Distributional Impact

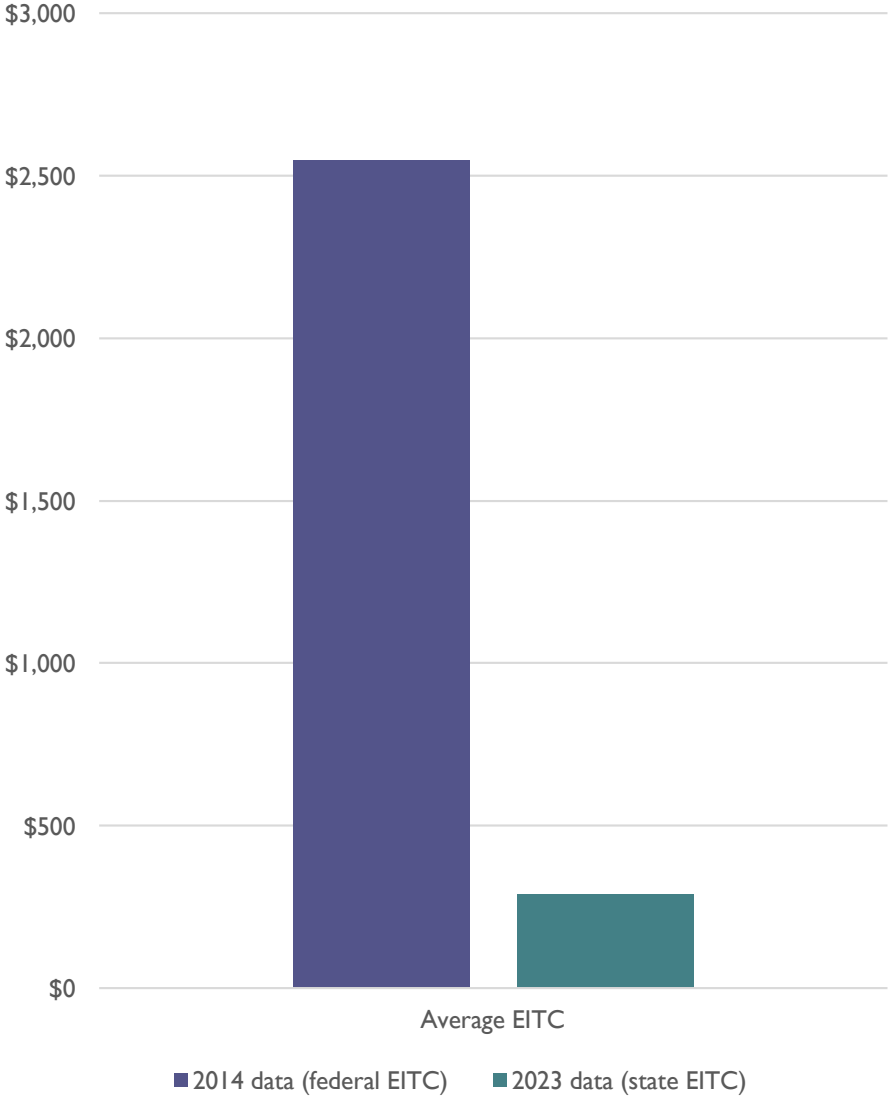
Refundable EITC Would Better Reflect Distribution of SC Gas Tax Increase

Tax change as percent of income by income group, if fully implemented in 2017



Source: Institute on Taxation and Economic Policy, May 2017

Scale of Federal to State EITC



Consider a separate goal...

- According to the IRS, the EITC participation rate in South Carolina in 2014 was 80.9%
- What happens if we increase participation by 5%?

Number of Claims in 2014	491,380
New claims if increase by 5%	24,569
Average amount of new claims (estimated at 50% of current average)	\$1,273
Total new claims	\$31,267,668

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