

Facts

About the Earned Income Credit:



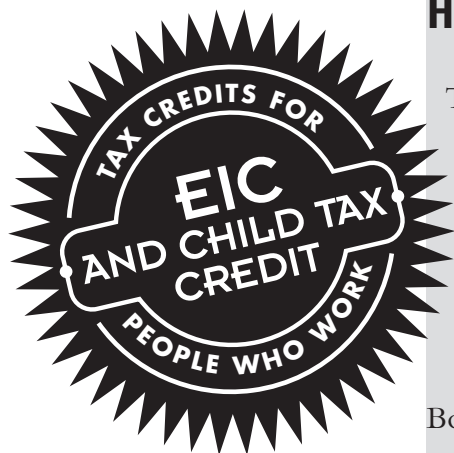
Tax Time
Can Pay for
Working
Families



**The Earned Income Credit
and Child Tax Credit**



Facts About the Earned Income Credit: Tax Time Can Pay for Working Families



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More Money for Workers in the District of Columbia, Illinois, Indiana, Kansas, Maryland, Massachusetts, Minnesota, New Jersey, New York, Oklahoma, Rhode Island, Vermont, and Wisconsin!

In addition to the federal EIC, low-income workers in these states can receive extra money for 2003 from a refundable state EIC. Because the state EIC is in addition to the federal credit, the EIC amounts you see in this kit will be lower than the combined federal and state EIC benefits available to workers in these states. Revise the materials in this kit to reflect the full amount of the EIC — federal and state — along with instructions for how to claim them. For more information, contact your state department of revenue.

Note: Colorado's state EIC is suspended for 2003 since the budget surplus that financed it is depleted; however, workers in Denver may still claim a city EIC. *For more information on state and local EICs, see the booklet in this kit "Making Tax Time Pay: How to Promote the Earned Income Credit and the Child Tax Credit."*

You don't have to be a tax expert to promote the Earned Income Credit!

Each year, community organizations, human services providers, businesses, employers, labor unions, government agencies, and a host of others find effective ways to incorporate Earned Income Credit (EIC) outreach activities into their routine operations. Most Outreach Campaign partners have no specialized tax knowledge — but they successfully alert working families and individuals about this critical tax benefit and direct them to free tax filing assistance. Their efforts mean millions of working families and individuals get a significant boost to their paychecks.

This booklet will help you get started.

This booklet provides the background you need to understand the basics of the EIC — who is eligible and how to claim it. In addition, you will find the answers to commonly asked questions and more

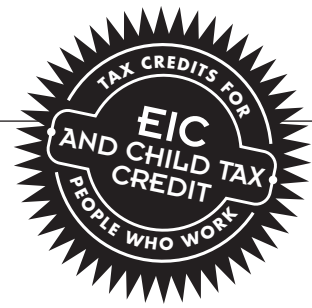
detailed information pertaining to special groups of eligible workers, such as members of the military or immigrant workers.

Many families can also get *Extra Credit* by claiming the Child Tax Credit.

Many working families can qualify for the Child Tax Credit and get up to \$1,000 for each child — in addition to the EIC for which they may qualify. You will want to get familiar with the Child Tax Credit, so you can help families take advantage of the full range of tax benefits. The rules for claiming the Child Tax Credit are different from the rules for claiming the Earned Income Credit. While this adds some complexity to the picture, the bottom line is that the outreach message to families can remain simple: ***Get all the tax credits you earned!*** For detailed information, a separate booklet, ***Facts About the Child Tax Credit***, is included in this kit.

The EIC Certification Pilot: The IRS will Test a New Eligibility Verification Procedure on 25,000 Claims in the 2004 Tax Filing Season

This year 25,000 workers who claim the EIC will be asked to submit verification with their 2003 tax return proving that their child lived with them for more than half the year. Only those tax filers selected by the IRS — a tiny fraction of those who claim the EIC — will be required to participate in this test. See the **Special Alert: EIC Certification Pilot**, enclosed in this kit for more detailed information about this pilot test and how Outreach Campaigns can assist workers in their communities who are affected.



The Earned Income Credit: Extra Money for People Who Work

What is the Earned Income Credit?

The EIC is a special tax benefit for working people who earn low or moderate incomes. It has several important purposes: to reduce the tax burden on these workers, to supplement wages, and to make work more attractive than welfare.

Workers who qualify for the EIC and file a federal tax return can get back some or all of the federal income tax that was taken out of their pay during the year. They may also get extra cash back from the IRS. Even workers whose earnings are too small to owe income tax can get the EIC. What's more, the EIC offsets any additional taxes workers may owe, such as payroll taxes.

Who can get the EIC and how much is it worth?

Single or married people who worked full-time or part-time at some point in 2003 can qualify for the EIC, depending on their income.

- Workers who were raising one child in their home and had family income of less than \$29,666 (or \$30,666 for married workers) in 2003 can get an EIC of up to **\$2,547**.
- Workers who were raising more than one child in their home and had family income of less than \$33,692 (or \$34,692 for married workers) in 2003 can get an EIC of up to **\$4,204**.
- Workers who were not raising children in their home, were between ages 25 and 64 on December 31, 2003, and had income below \$11,230 (or \$12,230 for married workers) can get an EIC up to **\$382**.

How does the EIC work?

- **Eligible workers can pay less in taxes and get a check from the IRS.** Mr. and Mrs. Johnson have two children, ages 20 and 21, in college. They earned \$29,000 in 2003 and owe the IRS \$730 in income tax, \$230 of which was withheld from their pay during the year. Their income makes them eligible for an EIC of

Which children qualify for the EIC?

- Sons, daughters, stepchildren, grandchildren and adopted children
- Brothers, sisters, stepbrothers, or stepsisters — as well as descendants of such relatives — if they were cared for as members of the family
- Foster children who are placed with the worker by an authorized government or private placement agency

"Qualifying children" must live with the worker for more than half of the year. (As of 2002, a full year is no longer required for foster children.) They must be under age 19, or under age 24 if they are full-time students. Totally and permanently disabled children of any age also may be qualifying children. Valid Social Security numbers are required for qualifying children born before December 31, 2003.

\$1,199. So, the EIC eliminates their \$730 income tax (now they don't owe IRS anything) and still gives them a refund of \$469.

- **Eligible workers can get a check from the IRS.** Cindy Williams has two children in college and earned \$19,000 in 2003. Her federal income tax for the year was \$285, which was withheld from her pay. She is eligible for an EIC of \$3,094. The EIC pays her back the \$285 she paid in income tax and gives her an EIC refund worth \$2,809. The IRS will send her a check for \$3,094.
- **Eligible workers who don't owe federal income tax can get a check.** Joe Smith has no children. He worked part-time in 2003 and earned \$5,200. Because of his low earnings he had no income tax taken out of his paycheck and owes nothing to the IRS. His earnings entitle him to an EIC check for \$382 (offsetting most of the payroll taxes that were withheld from his pay).

How do you get the EIC?

- Workers raising a "qualifying child" in 2003 must file either Form 1040 or 1040A and **must** fill out and attach Schedule EIC. Workers with children *cannot* get the EIC if they file Form 1040EZ or do not attach Schedule EIC. Married workers must file a joint return to get the EIC.
- Workers who were not raising a "qualifying child" in their home in 2003 can file any tax form — including the 1040EZ. These workers write "EIC" (or the dollar amount of their credit) on the Earned Income Credit line on the tax form. They do **not** file Schedule EIC.
- A correct name and Social Security number must be provided for every person listed on the tax return and Schedule EIC. If this information is incorrect or missing, the IRS will delay the refund.
- Workers don't have to calculate their own EIC; if they choose, the IRS will do it for them!

Workers raising children can get the EIC in their paychecks!

Workers who are raising children can get part of their EIC in their paychecks throughout the year and part in a check from the IRS after they file their tax return. This is called the Advance EIC payment option. *For more information, see "Boost Take-Home Pay! The Advance EIC Payment Option" on p. 9 of this booklet.*

Workers can get FREE help filing their tax forms

Many families that apply for the EIC pay someone to complete their tax forms. This can cost \$55 to \$100 or much more. Getting a "quick tax refund" that comes back in a few days costs even more. Paying for tax preparation takes away from the value of the EIC. But low-income workers can get free help with tax preparation through a program called VITA (Volunteer Income Tax Assistance). *For more information, see the booklet in this kit, "Helping Workers Claim the Tax Credits They've Earned."*

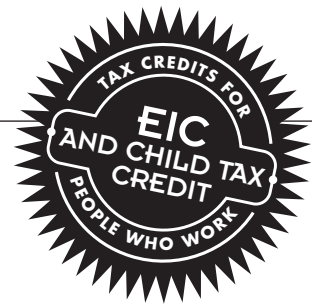
Does the EIC affect eligibility for other public benefits?

The EIC does not count as income in determining eligibility for benefits like cash assistance ("welfare"), Medicaid, food stamps, SSI, or public or subsidized housing. *For more information, see "Learn More: Questions and Answers About the EIC," on p. 11 of this booklet.*

Can immigrant workers get the EIC?

Many legal immigrants can qualify for the EIC, as long as they meet the eligibility requirements.

The materials in this kit should answer many questions about the EIC. *For more information, call the IRS at 1-800-TAX-1040.*



Rule Changes in Effect Since 2002

Simplify the EIC

Legislative changes make it easier for families to receive more money

As result of legislation passed by Congress in 2001, eligibility rules for the EIC were changed, simplifying the filing process and increasing refunds for many workers. Some workers who were previously ineligible for the EIC may now qualify.

Helpful Changes to the EIC:

1. Claims by custodial parents have priority.

Working parents living with relatives whose incomes are higher than their own may now benefit from the EIC. Before 2002, if a parent and grandparent lived together and could claim the same qualifying child (because the child could be claimed as the son of one or the grandson of the other), EIC eligibility went to the worker with the highest income. If the parent earned less than the grandparent, the parent's claim could be denied even if the grandparent chose not to claim the child for the EIC. If the grandparent's income exceeded the EIC eligibility limit, no one could claim the child for the EIC. Now, a parent's claim takes precedence over a claim by a non-parent. (However, if the parent chooses not to claim the EIC, another eligible relative living with the child can claim the credit.)

In the case of parents who do not file a tax return together, such as unmarried parents who each lived with the child for more than six months of the year, the parents may choose which one will claim the EIC. However, if both parents separately claim the child for the EIC, the IRS will award the EIC to the parent who lived the longest with the child,

or to the parent with the highest income if both parents lived with the child the same amount of time. (Remember that married parents must file a joint return to claim the EIC.)

Example: Rosita, who is 21, moved in with her mother last year after giving birth to her son because she could not afford a separate apartment on her low wages. Under the old EIC rules, Rosita would not have been able to claim her son for the EIC, since her mother earned more money than she did. The new rules allow Rosita to claim the EIC on her tax return even though her mother has higher earnings.

2. Six-month residency for foster children and relatives.

Under rules in effect before 2002, a brother, sister, stepbrother, or stepsister — or a descendant of such relatives, such as a niece or nephew — could be claimed as a foster child for the EIC if the child lived with the worker the entire year. A child who did *not* meet this relationship test also could be claimed if an authorized agency, such as a child welfare agency or court, placed the child with the worker and the child lived with the foster parent for the full 12 months of the year. Beginning in 2002, such relative children and foster children must live with the worker for “more than half of the year,” the same period of time as for *any* qualifying child. Also, the relative children described above are no longer considered in the “foster child” category for the EIC — placement by a foster care agency is not required.

Example: Barbara took in her nephew Antwan after her sister fell sick. He lived in her home since

March 2003. Since he lived with her for more than six months of 2003, she may claim him for the EIC. Previous rules would have prevented her from claiming Antwan because he did not live with her the entire year. If Antwan was *unrelated* to Barbara, she could claim him as a foster child, but an authorized agency would have to have placed Antwan with her.

3. Easier rules defining “earned income.”

Most EIC claimants have earnings only from work and are not likely to have other forms of income. However, in the past, if part of a worker’s earnings was non-taxable, such income also was considered in determining EIC eligibility and benefits.

Non-taxable earned income includes, for example, income that workers contribute to an employer-sponsored retirement plan or dependent care assistance plan. Housing and subsistence allowances for military personnel also are non-taxable earnings. Beginning in 2002, non-taxable earned income is no longer considered in determining eligibility for the EIC. This change simplifies the calculation of the EIC. Most workers affected by this change will receive a larger EIC benefit than they would have under the old rules. **Note:** Earned income does *not* include public benefits such as cash assistance or food stamps. Such benefits do not count as income in determining eligibility for the EIC.

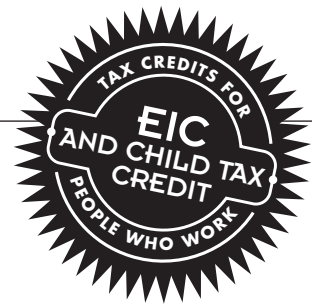
Example: Sally is a single parent raising two children. Sally’s job provides a dependent care assistance plan, allowing her to make pre-tax contributions toward the cost of child care, which are regularly deducted from her paycheck. Previously, Sally was required to add those non-taxable deductions back to her earned income, increasing her income for EIC purposes and reducing the amount of her EIC refund. Under the new rules, although her salary remains the same, Sally is not required to include those non-taxable deductions as earned income. Therefore, her income for EIC purposes is lower, and she will qualify for a larger EIC refund.

4. Standard adjusted gross income rules are used.

Adjusted Gross Income (AGI), which includes a worker’s earned and other taxable income, minus business and other losses, is used to determine a worker’s tax liability. However, in the past, EIC eligibility was based on “*modified AGI*,” which required workers to add back to their income 75 percent of business and other losses, as well as certain types of tax-exempt income. The resulting higher income level might then exceed EIC income limits and disqualify the worker, or reduce the amount of the EIC benefit for which the worker qualified. Beginning in 2002, the standard AGI definition will be used to determine EIC eligibility.

Example: Jason is a single parent of two and earned \$20,000 in 2003 working for an auto repair shop. He also started his own auto repair business from his home. He incurred a \$5,000 loss from his business, which he can subtract from his total income, making his Adjusted Gross Income \$15,000. The previous “*modified AGI*” rules would require Jason to add back 75 percent of the loss from his business (\$3,750), increasing his income for EIC purposes to \$18,750. Although Jason would still be eligible for the EIC, his refund would have been \$790 lower than it would have been if his business losses had been excluded. Beginning in 2002, the “*modified AGI*” rules no longer apply. Instead, the EIC uses regular AGI rules. This will make Jason’s tax return simpler. In addition, his income for EIC purposes will be \$15,000 (rather than \$18,750), qualifying him for a larger EIC refund than he would have received under the old rules.

*For more information on these eligibility rules, see IRS Publication 596, “Earned Income Credit,” for 2003 returns. It’s available for free by calling **1-800-TAX-FORM**, or download it from the IRS website at: www.irs.gov/formspubs.*



The EIC Can Help Low-Income Workers Not Living With Children

Very low-income workers who are not raising children in their home are eligible for a small Earned Income Credit. In tax year 2002, more than 3 million such workers received credits worth over \$660 million. The credit is available to people who worked full- or part-time in 2003 and:

- were at least age 25 and under age 65 on December 31, 2003;
- had earnings of less than \$11,230 (or \$12,230 for married workers);
- were *not* raising children their home who were under age 19 (or under age 24 if the child was a full-time student) for more than six months during 2003; and
- were *not* the dependent or qualifying child for the EIC of another taxpayer in 2003.

The credit for workers not raising children is worth up to \$382 for tax year 2003 — the average is expected to be about \$215. This credit works the same way as the EIC for families: it gives back some or all of the federal income tax taken out of a worker's pay during the year. The worker may also get additional cash back from the IRS. Even workers whose earnings are too small to have paid federal income tax can get the credit.

How do you get this credit?

Eligible workers not raising children get the EIC by filing a *federal income tax return*. They can use Form 1040, 1040A, or 1040EZ. On the "Earned Income Credit" line they simply fill in the amount of their credit or write "EIC" and the IRS will calculate the amount of the credit for them. Married workers must file a joint return to claim this credit.

Good News! If a worker doesn't fill in the credit amount or write "EIC" on the tax form, the IRS will automatically figure out if he or she appears to be eligible for the credit. If so, the IRS will send the worker a notice requesting additional information. The worker claims the EIC by submitting the additional information requested. Any refund owed to the worker will be received later in the year.

Phone it in! In 2003, over four million taxpayers filed their 1040EZ tax returns automatically by telephone. In 2004, this option will be available to single and married workers with no dependents who used the 1040EZ to file their tax returns in 2003 and are still at the same address. The IRS will send these workers a special "Telefile" packet with instructions and a special personal identification number (PIN). Using the tax forms and worksheets provided, taxpayers call the IRS Telefile number and key in the PIN and their tax form information. A touch-tone telephone is necessary. (Telefile is available for the hearing impaired who have access to TDD/TYY equipment.) *If the taxpayer is eligible for the EIC for workers not raising children, the credit will be calculated automatically.*

Why is the credit for workers not raising children important?

It provides a financial boost to those who work at very low wages or are only able to find part-time work. This includes many day laborers, migrant workers, temporary employees, homeless people and general assistance recipients who worked part of the year.

What do we know about the workers eligible for this credit?

Population statistics tell us about workers likely to qualify for this credit.

- The average annual earnings for these workers are about \$6,300. Two-fifths of them work in service industries. Almost 25 per cent work full-time, year round.
- Almost 80 percent of these workers have at least a high school diploma.
- The majority of these workers — approximately 61 percent — are non-Hispanic white. About 17 percent are African American and about 17 percent are Latino.
- Only about 15 percent are married. About 45 percent are single men and 40 percent are single women.

What are the special outreach challenges?

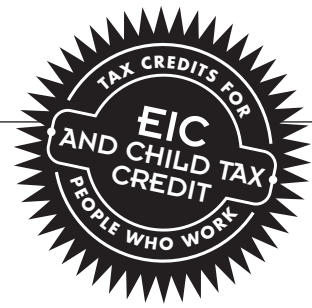
- For some, the EIC may seem too small to make filing a tax return worthwhile.
- Some may fear entering the tax system either because they haven't filed taxes in a long time or because they owe child support.

- Very low-income workers may be skeptical of information about programs from government agencies such as the IRS. Your outreach materials should contain the name and number of a contact organization that is trusted by low-income workers in your community.

Extra Credit for Non-custodial Parents

Lower-income workers whose children do not live with them may also qualify for the Child Tax Credit (CTC). A non-custodial parent who earned more than \$10,500 in 2003 may be eligible for a CTC of up to \$1,000 per child under age 17 claimed as a dependent on his or her tax return. Outreach messages that target this group of parents and highlight the CTC as a new opportunity are critical. *For more details on the CTC, see the booklet in this kit, "Facts About the Child Tax Credit."*

For more ideas on reaching workers not raising children likely to be eligible for the EIC, and those who might be able to claim the CTC, see p. 22 in the booklet in this kit, "Making Tax Time Pay: How to Promote the Earned Income Credit and the Child Tax Credit."



Boost Take-Home Pay!

The Advance EIC Payment Option

What is Advance EIC payment?

Most workers get the EIC in one large check from the IRS after they file a tax return. But there is another choice: employers can add part of a worker's EIC to every paycheck, and the worker gets the rest of the credit after filing a tax return. This is called "Advance EIC payment." Advance payments are not taxable income.

In 2004, Advance EIC payments are available to any worker with at least one qualifying child who expects 2004 income of less than \$30,338 (or \$31,338 for married workers). The credit for workers who are not raising children in their home is not available in advance payments.

What are the advantages of Advance EIC payment?

For many workers, getting part of their EIC in each paycheck can make a difference in paying the rent, buying groceries, and meeting other day-to-day needs. A worker earning between \$490 and \$1,300 a month, for example, can get about *\$50-\$60 extra in each bi-weekly paycheck*. Advance EIC payments are not counted as additional income in determining eligibility for public benefits such as cash assistance, housing assistance, food stamps and Medicaid. Employers also benefit from promoting Advance EIC payments — they can help employees increase their take-home pay at no cost to the business. This can decrease turnover in the workplace.

Protection against overpayment

Some workers decide against advance payments because they want a larger refund at tax time. But some workers also fear they will receive too much in advance and owe money back to the IRS after the end of the year. However, the advance payment procedure has built-in protections against overpayment. Workers who choose advance payment can get up to about half of the EIC amount to which they're entitled for the year. They get the rest as a refund when they file their tax return. This means workers can get advance payments *and* a year-end refund! And, because workers receive only part of their EIC during the year, they're protected against getting too much in advance and owing some back at the end of the year.

Some workers should not choose Advance EIC payment

Eligibility for Advance EIC payments is based on the total income a worker expects to earn in a year, including the income of a spouse. Major changes in family income, marriage or the eligibility of a qualifying child during the year can decrease the EIC for which workers are eligible. If a worker continues to receive advance payments based on an incorrect estimate of eligibility, these payments may exceed the amount of the EIC. In this case, the worker would have to send the IRS a check at tax time to make up the difference.

The following workers should not use the advance payment option:

- Workers who hold two or more jobs simultaneously
- Workers with a working spouse, unless both spouses take advance payments during the year (*For more information, see the next section.*)
- Workers who get married during the year, if both spouses work
- Workers whose earned income increases a lot

How do you get the Advance EIC payment?

To get the Advance EIC eligible workers fill out a **W-5 form** called the “Earned Income Credit Advance Payment Certificate” and give part to their employer. The W-5 is available from employers. The W-5 form may be photocopied and distributed. *The W-5 form for 2004 is available for free by calling 1-800-TAX-FORM, or download it from the IRS website at: www.irs.gov/formspubs.*

Eligible workers can file a W-5 at any time during the year, but then they must file a *new* W-5 at the beginning of each new year to continue getting the EIC in their paychecks.

Married workers can choose advance payment, but if they do, *both spouses should give a W-5 to their employers*. The box on the W-5 indicating the worker’s spouse also has a W-5 in effect should be checked “yes.” This signals the employer of each spouse to figure the correct amount of the advance payment and avoid an EIC overpayment. If only one spouse chooses advance payment, the amount he or she receives may be too high.

A worker already receiving Advance EIC payments who is planning to get married to someone who also works, or expects a large pay increase during the year, should ask his or her employer to stop

the advance payments. To do this, workers file a new W-5 form with their employer and indicate they don’t want to receive advance payments any more.

Remember! Workers who get Advance EIC payments during the year must file a tax return after the end of the year and fill in the correct line to show the total amount received in advance payments. They must also complete Schedule EIC and attach it to their tax return.

Some workers aren’t eligible to get Advance EIC payments

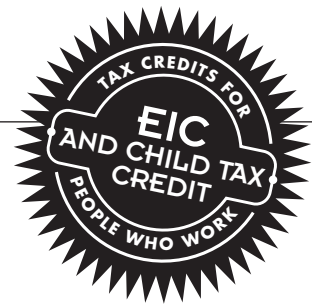
Some workers who are eligible for the EIC are not allowed to get advance EIC payments, including:

- Workers without qualifying children
- Workers who get paid day by day
- People with no Social Security and Medicare taxes withheld from their pay
- Self-employed workers, who cannot advance the EIC to themselves

What is the employer’s role?

Advance payments don’t cost employers money. Employers simply subtract the advance payments they have added to their workers’ paychecks from the total taxes withheld from all employees they would otherwise deposit with the IRS. Most automated payroll systems handle Advance EIC.

Some employers may not be aware of the Advance EIC payment option. But under federal law, any eligible employee who files a W-5 must be given advance payments. Employers are not required to make sure employees are eligible for the EIC — that is the employee’s responsibility. *For more information, see the IRS “Employer’s Tax Guide, Circular E,” available free by calling 1-800-TAX-FORM, or from the IRS website at: www.irs.gov/formspubs.*



Learn More: Questions and Answers About the EIC

People often have questions about whether they can qualify for the EIC. This fact sheet provides the answers to many commonly asked questions, including questions about how the EIC affects public benefits, college aid, eligibility for non-traditional families, disabled workers, military families and immigrants, as well as how to claim the EIC for past tax years.

EIC and Public Benefits

Can people who work and also get welfare benefits, still get the EIC?

Yes. As long as they earn wages and meet the income and other eligibility requirements. These workers may use the Advance EIC payment option, if they wish.

Note: Some welfare recipients are required to participate in “work experience” and “community service programs” (often called “workfare”) in exchange for their cash assistance benefits. These benefits are not counted as income to determine eligibility for the EIC. However, current or former recipients who are employed in private or public sector jobs for which employers are subsidized through state welfare block grants or other government programs do earn wages that count in determining eligibility for the EIC. *For more information, contact the Center on Budget and Policy Priorities, (202) 408-1080.*

Will getting the EIC lower other government benefits? Could someone lose benefits altogether?

Generally, no. Under federal rules, the EIC (including advance payments) is not counted as income for Medicaid, food stamps, SSI or federally assisted housing programs. The EIC must be spent by the end of the month after the month in which it is received or it can count as a resource in determining eligibility for SSI or Medicaid. Often, if the recipient has few or no other resources, saving part of an EIC refund is not enough to cause that recipient to exceed the resource limit for the benefit programs mentioned. Many states now have no resource limit for families on Medicaid; that is, they do not count assets in determining eligibility. Thus, saving an EIC refund would not affect eligibility for Medicaid in those states. The EIC can count as a resource in determining eligibility for food stamps if it is not spent within 12 months of receiving the refund.

Note: Deposits in certain types of Individual Development Accounts (IDAs), which may include some of a worker’s EIC refund, do not count as a resource in determining eligibility for the above programs or for state cash assistance programs. *For more information, see the fact sheet on p. 21 in this booklet, “The EIC Can Help Multiply Assets.”*

The welfare legislation enacted in August 1996 replaced the AFDC program with a block grant called Temporary Assistance for Needy Families (TANF). Under the block grant, each state can set its own rules for how the EIC will be treated in determining eligibility for cash assistance. Other

than Alabama, no state counts the EIC refund as income to determine eligibility. However, in Connecticut, Advance EIC payments may in some circumstances affect a worker's TANF eligibility. Generally, state TANF programs adopted the rule that the EIC must be spent by the end of the month after the month in which it is received or it can count as a resource. However, some states may have adopted less restrictive policies. *Contact your state welfare agency for the rule in your state.*

Rules on how the EIC may affect "General Assistance" benefits are different in each state where a general assistance program is in place. *Contact your state or local welfare agency for information.*

How to Claim Back EICs and Other Filing Questions

What if a worker was eligible for the EIC in past years but didn't claim it?

Workers can file for the EIC for the last three years. For example, a worker who was eligible for the EIC in 2000 but did not claim it can fill out a Form 1040X, "Amended U.S. Individual Income Tax Return," and attach it to a copy of the 2000 tax return he or she filed that year. Workers claiming a child for the EIC also must fill out and attach Schedule EIC for 2000. *For copies of prior-year forms, call 1-800-TAX-FORM. For more information, see p. 16 in the booklet in this kit, "Helping Workers Claim the Tax Credits They've Earned."*

What happens if a worker files for an EIC and the IRS finds out that taxes are owed?

The worker must pay whatever is owed. **But:**

- The EIC may be enough to cover the taxes owed.
- The IRS is usually willing to work out payment plans for back taxes.
- The worker may be able to make an "offer in compromise" that is less than the tax bill.

What about workers who did not file a return and discover they had been eligible for the EIC?

An eligible worker can file a return and claim the EIC for three back years. For example, in 2004 workers are filing taxes for 2003. If a worker failed to file or claim the EIC in the past, he or she could still file for 2002, 2001 and 2000. A worker must file a separate return for each prior year and, if claiming a child for the EIC, also fill out and attach the Schedule EIC for that year. A Form 1040X is not required. There is no late filing penalty, unless the worker owed income tax in the prior year. The amount owed the IRS will be deducted from the EIC. Workers who may owe taxes in excess of their EIC should seek assistance from a Low Income Taxpayer Clinic, accountant, or attorney and, if necessary, arrange a payment agreement with the IRS.

Will the IRS require additional information beyond what a worker provides with his or her tax return?

Generally, the IRS will not require any additional information. But, if information provided on the tax return or Schedule EIC seems questionable, the IRS may request additional documentation to verify the EIC claim. In such cases, the IRS will

send the filer a questionnaire that specifies the type of documentation that must be submitted. For example, a filer may be asked to submit a copy of a qualifying child's birth certificate. It is important that the name on the birth certificate match the name on that child's Social Security card. If a child is over age 24 and permanently and totally disabled, proof of disability status could be requested. The IRS also may require documents verifying that a qualifying child actually lived with the filer at least half the year (or a full year if a foster child, for years prior to 2002). Filers claiming the EIC should *not* mail in any additional documentation with their tax returns unless such documentation is specifically requested by IRS. If additional information is requested, filers need submit only the documents specified. **Exception:** Workers whose EIC claim was disallowed in a previous year, but who now claim they are eligible, must attach Form 8862, "Information to Claim Earned Income Credit After Disallowance," to their tax return in order to submit a new claim.

Workers who are in the pilot test group for EIC Certification are required to submit an additional tax form and supply additional documents to submit an EIC claim. For more details, see the Special Alert: EIC Certification Pilot enclosed in this kit.

Can self-employed workers get the EIC?

Yes. They will need to fill out additional forms to accompany their Form 1040 and Schedule EIC (if they were raising children in their home): Schedule C, "Profit or Loss from Business," (or Schedule C-EZ) and Schedule SE, "Self Employment Tax," (if their self-employment income is more than \$400). *Call the IRS at 1-800-TAX-FORM to get the necessary forms or download them from the IRS website at: www.irs.gov/formspubs.*

EIC and Social Security Numbers

Who needs a Social Security number?

Valid Social Security numbers must be provided for everyone listed on the tax return, *including infants born before December 31, 2003*. Only valid Social Security numbers issued to U.S. citizens or Social Security numbers issued to non-citizens who have permission to work legally in the United States are acceptable. *For more information see p. 14 of this booklet.* The IRS now verifies the Social Security number of every adult claiming the EIC, as well as the Social Security number of every child in families claiming the EIC, before it sends out EIC payments. The IRS also checks to make sure that no child is claimed more than once.

The processing of an EIC claim and the receipt of any refund will be delayed if the tax return or Schedule EIC is incomplete or contains incorrect information. Workers who file paper returns with missing or mismatched Social Security numbers will be sent a notice by the IRS stating that the return was incomplete and requesting that the missing information be mailed in. This can delay processing several weeks. Electronically-filed returns will be rejected by the IRS computer if a Social Security number is missing or the name and number do not match. The corrected return must then be filed as a paper return.

It also is important to be sure that each name and Social Security number is recorded on the tax return *exactly* as it appears on the person's Social Security card. For example, if a woman records her married name on the tax return, but her Social Security card bears her maiden name, the discrepancy will need to be resolved before the tax return can be processed. (To avoid such an error, the woman can apply to the Social Security Administration to have her name changed on her Social Security card. Correcting this discrepancy

also will help ensure that Social Security taxes are being deposited in the proper account.)

Workers who don't have Social Security numbers for their children by the tax filing deadline can still get the EIC by:

- Filing their tax return without claiming the EIC and then, after receiving the Social Security number, filing an “amended return” (Form 1040X) and attaching Schedule EIC, OR
- Filing Form 4868 to request an extension on their tax filing deadline to August 15. *To have an application for a Social Security number sent to your home, call 1-800-772-1213. Or call the Social Security Administration in your state to find out how to apply.*

EIC and Immigrant Workers

Can immigrant workers get the EIC?

Many legal immigrants who are employed can get the EIC. The changes in federal law in 1996 that denied public benefits such as food stamps and SSI to many legal immigrants did not apply to the EIC. *In order to claim the EIC, immigrant workers, their spouses, and children listed on Schedule EIC must each have valid Social Security numbers that permit them to work legally in the United States.* Individual Taxpayer Identification Numbers (ITIN) issued by the IRS to non-citizens, and non-work Social Security numbers issued to applicants or recipients of federally funded benefits programs cannot be used to claim the EIC. (**Note:** An ITIN can be used to claim the Child Tax Credit refund. *See the booklet in this kit, “Facts About the Child Tax Credit.”*)

In addition, an immigrant must be a “resident alien for tax purposes” for the entire tax year to claim the EIC. An immigrant who was a non-resident

alien at any time during the year cannot claim the EIC unless he or she:

- was married to a U.S. citizen or a resident alien as of December 31 of the tax year, and
- files a joint tax return with the spouse and chooses to be treated as a resident alien for the entire year.

For more information on how resident alien status is determined, see IRS Publication 519, U.S. Tax Guide for Aliens.

Immigrants who are “resident aliens for tax purposes” may be legal permanent residents, meaning they have a “green card” (I-551 card). However, many legal immigrants who do not yet have their “green cards” may still be resident aliens for tax purposes. For example, the following immigrants might qualify for the EIC *if they and family members have legal work authorization and Social Security numbers:*

- Amnesty temporary residents and amnesty family members granted “Family Fairness” or “Family Unity” status
- Refugees, asylees and those granted Temporary Protected Status
- Applicants for these and other immigration statuses who have legal work authorization and Social Security numbers.

Remember! Immigrant workers’ children must have lived with them in the United States for more than six months of the year to be considered qualifying children for the EIC. Also, the worker’s main home must be in the United States.

Can immigrant workers get the Advance EIC payment?

Generally, yes. But some workers (whether they are immigrants or not) are not allowed to use the

Advance EIC. They include workers who get paid day-by-day and workers whose employers don't withhold Social Security and Medicare taxes from their pay.

Can immigrant workers who obtain legal work status claim the EIC for a previous year?

Workers who otherwise met all the EIC eligibility requirements in previous years, and later obtain legal work status from the U.S. Immigration and Naturalization Service (INS), may be able to claim the EIC for up to three previous years. A worker's spouse or qualifying children, if any, must also have legal work status. After receiving legal work status from the INS, the worker, spouse and qualifying children must obtain Social Security numbers. Such workers may claim the EIC by amending their tax return for the previous year, even if they had been denied the EIC in that year because they had not yet obtained a valid Social Security number. Or workers can file an original return for the previous year if they had not already done so. *For more information see IRS National Office Chief Counsel Advice Memorandum, CCA 2000028034, "Claiming Previously Denied Earned Income Credit due to Invalid Social Security Numbers," June 9, 2000. Contact the IRS at (202) 622-6060.*

Does getting the EIC cause problems for immigrant workers?

The EIC does not create "public charge" problems for immigrant workers. Receiving the EIC is not considered an indication that the immigrant is unable to support him- or herself financially.

In general, information on a tax return is confidential. The IRS cannot share tax return information with the Immigration and Naturalization Service. There are exceptions in cases involving federal criminal or terrorism investigations or when the IRS thinks someone is breaking a tax law.

For more information about which immigrant workers qualify for the EIC, how to obtain Social Security numbers and other immigrant tax issues, call the National Immigration Law Center at (213) 639-3900.

EIC and Non-Traditional Families

EIC eligibility rules in effect since 2002 give parents priority in claiming the EIC. A working custodial parent can claim the EIC even if he or she is living with another relative who earns more.

What are the rules about filing status?

To get the EIC, workers can file as: "single," "head of household" or "married filing jointly." But the EIC is not available to taxpayers who file as "married filing separately."

What if parents are separated but not divorced?

Parents who are separated but not divorced often file as "married filing separately." But if they file this way, neither parent can claim the EIC. Separated parents have the option of filing as "married filing jointly." If they do so, they can claim the EIC.

In addition, there is *one* situation in which a separated parent can claim the EIC but not have to file jointly with the other parent — the parents must have lived apart for the last six months of the year **and** their child must have lived with one of them for more than half of the year. **Also**, the parent now living with the child must have paid more than half the cost of maintaining the household for the year and be able to claim the child as a dependent. Under these circumstances, that parent is considered unmarried for tax purposes and can file as "head of household." That parent may claim the EIC. This option can be important, for example, to workers who are

victims of domestic violence or whose separated spouse is not cooperative.

What if the parents in a family are divorced?

If parents are divorced, the parent with whom the child lived for more than half the year is entitled to file for the EIC, regardless of which parent claims the child as a dependent. If *both* parents lived with the child for more than six months, either parent could claim the EIC, and the parents should decide which one will. However, if each parent separately claims the child for the EIC, the IRS will determine which parent lived the longest with the child and will deny the claim filed by the other parent. If the child lived with both parents for the same amount of time during the year, then the parent with the highest adjusted gross income is entitled to the EIC. (**Note:** A parent not living with his or her child for more than half the year may be eligible for the smaller EIC for workers without qualifying children.)

What if both parents and their child live together, but the parents are not married?

If the parents are not married, and each lived with the child for more than six months, either parent may claim the EIC based on that parent's income. Since they are unmarried, they do not file a joint return. However, if each parent separately claims the EIC, the IRS will award the EIC based on which parent lived with the child the longest and deny the claim of the other parent. If the child lived with both parents for the same amount of time during the year, then the parent with the highest adjusted gross income is entitled to the EIC.

What about a three-generation household: a grandparent, parent and child?

In a three-generation household, only one person can claim the EIC, even if more than one family member works and has an income that would qualify for the credit. Under rules in effect since 2002, the child's parent has the priority to claim the EIC. If the parent chooses not to claim the credit, an eligible grandparent may claim it. (In a household with no working parent and more than one relative who could claim a child, relatives may decide who will claim the EIC. However, if more than one worker claims the same child, the IRS will award the EIC to the person with the highest adjusted gross income.)

What about child support?

Child support payments a parent receives do not count as income when determining eligibility for the EIC or the amount of the EIC.

What about foster families?

A new rule in effect since 2002 changed the definition of a foster child for purposes of the EIC. Under this rule, a child must be placed with the worker by an authorized placement agency, such as a licensed foster care agency, state agency or court. Such children must live with the worker for more than half of the tax year and meet the EIC age requirements for a qualifying child. (If the child is totally and permanently disabled he or she can be any age.)

Foster care payments generally do not count as income when determining eligibility for the EIC. Since such payments *can* affect a foster parent's ability to claim a foster child as a dependent, foster parents may mistakenly think this jeopardizes their EIC claim. However, in general, the IRS does not require children to be claimed as dependents in

order to be claimed for the EIC. (However, a child must be claimed as a dependent to be claimed for the Child Tax Credit.) *For more information, see “Federal Tax Benefits for Foster and Adoptive Parents and Kinship Caregivers” at: www.casey.org/cnc/publications.htm and the booklet in this kit, “Facts About the Child Tax Credit.”*

Note: Under rules in effect before 2002, a brother, sister, stepbrother, or stepsister — or a descendant of such relatives, such as a niece or nephew — could be claimed as a foster child for the EIC if the child lived with the worker the entire year (placement of the child with the worker by an official agency was not required for such related children). Under the new rules, in effect since 2002, such children may be considered qualifying children for the EIC if they live with the worker for more than half of the year. These qualifying children are no longer considered in the “foster child” category for the EIC. EIC claims for a year prior to 2002 must follow the eligibility rules that were in effect for that year.

EIC and Disabled Workers

Can a person who receives disability benefits get the EIC?

A person who receives long-term, *employer-paid* disability benefits and is under minimum retirement age can qualify for the EIC, even if he or she did not work during the tax year. (Minimum retirement age is considered to be the earliest age at which a worker can receive a pension or annuity if he or she is not disabled.) Such disability benefits are considered taxable income, are reported as wages on tax returns, and are considered earned income for purposes of the EIC.

Benefits from Social Security Disability Insurance, SSI, and payments from individually-purchased disability insurance policies are not counted as

earned income. To be eligible for the EIC, individuals who receive these types of benefits also must have earned income.

A worker may claim a totally and permanently disabled person of any age as a “qualifying child” for the EIC if that person otherwise meets the qualifying child requirements for the EIC. In some cases, a totally and permanently disabled person may be eligible to claim the EIC. However, that person is not eligible to claim the credit if he or she can be claimed as a qualifying child by another worker. Also, if the disabled person is claimed under the EIC foster child provisions described in the previous section, an authorized agency must have placed the disabled person in the care of the worker.

EIC and College Financial Aid

College students who also work and are raising children may be eligible to claim the EIC. Students between ages 25 and 64 who are not raising children and who work may also be eligible. Parents of full-time students under age 24 may also be able to claim the EIC.

- Non-taxable scholarships and grants are *not* considered income in determining eligibility for the EIC; *taxable* grants and scholarships also are not considered “earned income,” but are included in determining “adjusted gross income,” which may affect eligibility for the EIC.
- An EIC refund is counted as family income in determining financial aid eligibility. However, for many low-income students who work, or their parents, the EIC will have no effect on financial aid amounts or eligibility. *For more information, contact your college’s financial aid office.*

For information on which scholarships and grants are taxable or non-taxable, call the IRS at 1-800-829-1040. For ideas on outreach to students, contact the Center on Budget and Policy Priorities at (202) 408-1080 or at www.cbpp.org/eic2004 to obtain the fact sheet, “Ten Ways Your College or University Can Promote the EIC.”

Can Military Personnel Claim the EIC?

Members of the military assigned overseas may wonder about their eligibility for the EIC. Military personnel can claim the EIC (and the Child Tax Credit), whether they live in the United States or overseas. Also, under a new definition of “earned income” in effect since 2002, more members of the military may qualify for the EIC or receive a larger benefit.

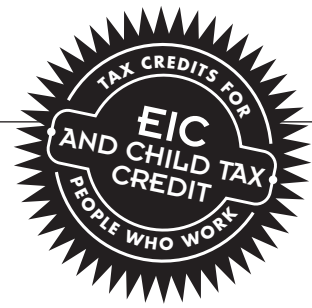
Military personnel who live with qualifying children while stationed on active duty outside the U.S. can be eligible for the EIC. Even if the qualifying children of a member of the military who is stationed overseas remain in the U.S., they may be claimed for the EIC. This is because IRS considers an individual assigned to an overseas tour of duty to be temporarily absent from the U.S. due to a special circumstance. The length of time the person is absent is treated as though he or she was in the U.S., as long as the individual plans to return to his or her main home in the U.S. at the end of the military assignment. Military couples living apart due to military assignment must still file a joint return to receive the EIC.

An individual in the military under age 19 may be claimed as a qualifying child. If such an individual is temporarily absent due to an overseas military assignment, he or she still may be considered a qualifying child as long as he or she intends to return home at the end of the military assignment.

Under new rules in effect since 2002, non-taxable combat pay and allowances for housing and subsistence — including the value of meals and lodging furnished in-kind to personnel residing on military bases — *are no longer considered earned income* for EIC purposes. Such pay and allowances are indicated on W-2 forms, but no longer are added to regular wage income to calculate eligibility for the EIC. In many cases, this will result in a larger EIC refund since the amount of earned income considered for the EIC is reduced. The purpose of this rule change was to simplify claiming the EIC.

Veterans’ benefits and military retirement pay are not considered earned income.

For further information on EIC rules for military personnel, see IRS Publication 3 “Tax Information for Military Personnel (Including Reservists Called to Active Duty).”



Making the Case: Talking Points on the EIC

As you work on your Outreach Campaign, you will come in contact with people who don't know a lot about the EIC and why it is important.

These “talking points” will help you answer questions about the EIC. They can be useful when you are advocating for the EIC with community leaders, with organizations you want in your campaign or with businesses and funders. They can also be helpful in preparing remarks for the media.

Why is the EIC important?

- The EIC is a federal tax benefit designed to help low-income workers increase their financial stability. It has several important purposes: to reduce taxes for these workers, to supplement wages, and to make work more attractive than welfare.
- The EIC is a federally funded, anti-poverty initiative that helps working people maintain their independence from the welfare system. Data from the U.S. Census Bureau, Current Population Survey, indicate that in 1999, the EIC lifted 4.7 million people — including 2.6 million children of low-income workers — above the federal poverty line.
- In 2003, over 21 million working families and individuals received the EIC. Yet research indicates that 15 to 20 percent of those who are eligible each year fail to claim their credit, either because they are unaware of it or cannot obtain the help they may need to file a tax return.

- The EIC takes on added importance during an economic downturn. Families that have lost income badly need the boost the tax credits provide. The EIC can provide relief for families under severe economic stress, enabling them to pay back bills, avert utility shut-offs or eviction, buy groceries, and cover child care costs and other work-related expenses.

Who benefits from the EIC?

Working families with children

- Children are more likely to be poor than Americans of any other age group. The largest EIC benefit is for working families with two or more children.
- Raising children is expensive. The EIC can help offset the costs of child care, clothing, school supplies, and other needs.

Low-income workers who do not have a qualifying child

- This credit provides a financial boost to people who work at very low wages or are only able to find part-time work: day laborers, migrant workers, temporary employees, homeless people, general assistance recipients who worked part of the year and others. About 3.5 million workers received this credit for tax year 2002.

State and local economies

- EIC participation boosts state and local economies. In the first eight months of 2003 alone, over \$37 billion in federal EIC funds flowed into the states.
- Since most EIC benefits are spent locally, the EIC is an economic development tool for low-income neighborhoods.

Businesses

- Helping customers get the EIC is a legitimate and important business activity. Surveys have found that 80 percent of EIC recipients plan to use their credit to help pay immediate bills, such as rent or utilities, or to pay for better housing, transportation or educational needs. The Advance EIC payment option can help workers stay current with their monthly household bills.
- Businesses make a valuable contribution to their communities by promoting the EIC.
- EIC benefits increase the take-home pay of employees at no cost to the business. Helping employees support themselves and their families can reduce turnover in the workplace.

Other important issues related to the EIC

The EIC is different from welfare

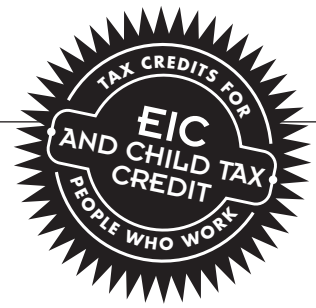
- When welfare recipients get a job, their benefits are likely to shrink or disappear. In contrast, the EIC rewards people who find and keep a job by adding to the wages they earn.
- The EIC does not require an interview with a caseworker or a trip to a government office. Eligible workers apply by filing a tax return.

Free tax preparation and refund anticipation loans

- When low-income people pay to have their taxes prepared, the value of their EIC is diminished. This undermines the basic objectives of the EIC.
- IRS data indicate that 68 percent of EIC recipients pay someone to prepare their tax returns. Fewer than one in 10 have their tax forms prepared for free by VITA (Volunteer Income Tax Assistance). Increasing awareness about VITA and improving access to these services is critical.
- Many people who use commercial tax preparers to get a refund anticipation loan — a “quick refund” they receive in just a few days — don’t realize that what they’re paying for is a very high-interest loan from the tax preparer. *For more about this issue, see p. 5 in the booklet in this kit, “Helping Workers Claim the Tax Credits They’ve Earned.”*

Immigrant workers

- Recent immigrants are often the poorest members of our communities. They work at jobs that pay low wages and struggle to support themselves and their families. Changes in federal law made some legal immigrants ineligible for public benefits such as food stamps and Medicaid. *But these rules did not affect EIC eligibility — legal immigrant workers may still qualify for the EIC.* For these reasons, educating immigrant workers about the EIC is important. *For more on this issue, see p. 14 of this booklet.*



The EIC Can Help Multiply Assets

Individual Development Accounts (IDAs) have emerged in the last few years as a new way for low-wage workers to develop a substantial savings account. IDAs are “matched savings accounts,” in which savings deposits made by a worker are matched by contributions from IDA program funds. Organizations administering IDA programs use federal or state funds authorized for IDAs, and additional funds from foundations and financial institutions, to supply the match.

IDA accounts are designed to enable workers to obtain a valuable asset, such as a down payment on a home, college education, job training, a computer, a car, or small business financing. Low-wage workers often experience great frustration with the long time it takes to save enough to meet these goals. The matched savings feature of IDA accounts responds to this concern by helping depositors build their savings more quickly.

A limit is generally placed on the amount workers may deposit each year and also on the total amount that can be deposited. Since IDA programs are supported by a variety of sources and administered locally, the match rates and maximum deposit rules vary by program.

How the EIC Fits In

Even with the enticement of matching contributions, low-income workers may have difficulty saving part of their wages for long-range goals. EIC refunds — and Advance EIC payments in worker paychecks — can make it more feasible for them to make the modest monthly deposits

typically required in an IDA program. EIC refunds themselves are permitted to be deposited in IDA accounts.

A recent study of EIC recipients by the Center for Policy Research at the Maxwell School, Syracuse University, found that almost one-half of those surveyed said they planned to save some or all of their EIC refund check, rather than use it all to pay bills or make immediate purchases. Respondents mentioned asset-building goals, such as paying tuition or purchasing or repairing a car, as priority uses for their EIC.

The IDA match can multiply a worker’s own savings — doubling, tripling or even quadrupling the amount they deposit, depending on the IDA program and the purpose for which the worker has designated the IDA account.

For example, the weekly take-home pay of a full-time worker with three children who earns \$7 per hour (about \$14,500 per year) is about \$250. If the worker saves five percent of his or her weekly take-home pay — about \$12 each week or nearly \$50 each month — the annual savings comes to \$624. Over three years, the worker will have saved \$1,870. But, in an IDA account that matches two dollars for each dollar saved by the worker, those savings multiply to more than \$5,500, not counting interest on the account.

While this worker might struggle to save \$50 per month, the EIC can help take the pressure off. For work in 2003, this person could be eligible for an EIC worth over \$4,204 and a Child Tax Credit

refund worth \$400. He or she could also opt to receive Advance EIC payments totaling nearly \$100 in additional take-home pay each month and using some or all of the extra cash to make deposits into an IDA account.

Some Asset Development Programs

Asset development programs for low-income workers are taking hold around the country. Following are some of the most notable and how to find out more about them.

Two organizations lead national efforts to develop IDA programs and other asset development policies: The Corporation for Enterprise Development in Washington, D.C. at (202) 408-9788, and the Center for Social Development, at Washington University, St. Louis, Missouri at (314) 935-7433. Their websites are provided below.

The IDA network. Successful federally supported IDA demonstration programs, such as the Assets for Independence Act (AFIA) administered by the U.S. Department of Health and Human Services, have spurred a rapidly growing network of organizations that administer IDA programs. IDA programs already exist in about 350 communities across the nation. *For more information, visit the Corporation for Enterprise Development website at: www.cfed.org.*

IDs for people who receive public benefits.

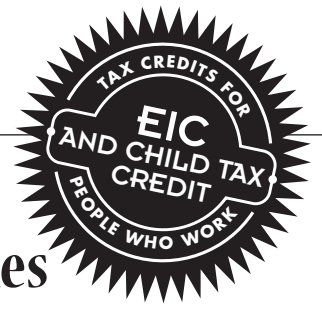
Federal welfare law permits states to design IDA programs to benefit welfare recipients beginning the transition to employment. States may use their TANF block grant funds to support IDA programs. Individual savings and matching contributions in accounts under IDA programs which meet the requirements of federal welfare law (or IDs in the AFIA demonstration program) do not affect a person's eligibility, or benefit amount, for cash assistance and other public benefit

programs. Assets in other types of IDs, however, are not necessarily excluded as a resource in determining eligibility for benefit programs such as welfare or food stamps. *For more information, see the "2002 Federal IDA Briefing Book: How IDs Affect Eligibility for Federal Programs" by the Center on Budget and Policy Priorities and the Corporation for Enterprise Development at: www.cbpp.org/10-29-02wel.pdf. For information and contacts regarding specific state IDA policies, visit the website of the Center for Social Development at: gwweb.wustl.edu/csd/statepolicy.*

IDs for refugees. The Office of Refugee Resettlement (ORR) under the U.S. Department of Health and Human Services provided grant funding in 2003 for 49 nonprofit organizations in 19 states to develop IDA programs for low-income refugees. *For more information about the Refugee Individual Development Account Program, contact Lisa Campbell, Office of Refugee Resettlement, (202) 205-4597 or lcampbell@acf.dhhs.gov.*

Family Self-Sufficiency Program (FSS).

FSS is a program that promotes employment and saving among families that have Section 8 housing vouchers or live in public housing. Under FSS, a tenant agrees to reach certain employment and training goals. Usually, as the tenant earns more from employment, her rent payments will increase. But the FSS participant can get a refund of some or all of her increased rental charges in an amount equal to about 30 percent of her increased income. This amount is deposited by the housing agency into an FSS escrow account established for the tenant and HUD reimburses the agency for the escrow deposits. When the tenant meets the goals of the FSS agreement, she receives the full amount in the escrow account, plus interest. Some families accumulate as much as \$10,000 in their escrow accounts; the average received by families that complete the program is nearly \$5,000. *For more information, see "The Family Self-Sufficiency Program" at: www.cbpp.org/4-12-01hous.htm.*



Saver's Tax Credit for 2003: Workers Can Save for Retirement And Reduce Income Taxes

The Saver's Tax Credit can reward workers who make contributions to a retirement plan or Individual Retirement Account (IRA). Workers can receive a tax credit worth up to 50 percent of a maximum \$2,000 contribution. Married workers may each make the maximum contribution. The Saver's Tax Credit, is referred to in IRS tax forms as the "Credit for Qualified Retirement Savings Contributions. This may be particularly valuable for workers in areas where matched-savings plans, such as Individual Development Accounts (IDAs), are not available or when saving for retirement is a higher priority for a family than the uses that may qualify for matched savings in an IDA.

The Saver's Tax Credit will reduce or eliminate a worker's income tax but, unlike the Earned Income Credit, workers who owe no income tax will not benefit from the Saver's Tax Credit. However, some moderate-income workers with children may see increased benefits from the EIC when they make contributions to a retirement account through pre-tax salary deductions and take advantage of the Saver's Tax Credit. Here's why:

- Non-taxable earned income is no longer counted in figuring the EIC. Most EIC claimants who also make contributions for retirement through pre-tax salary deductions are in the "phase-down" range of the EIC, where EIC amounts decrease as taxable income increases. Since the salary deductions made for retirement reduce the worker's taxable income, the worker will qualify for a larger EIC.

- The Saver's Tax Credit reduces or eliminates the income tax a worker may owe. If that worker also qualifies for the new Child Tax Credit, less of that credit will need to go toward reducing income tax liability and more will be available for a refund to the worker.

Example: Randy and Meg earned \$25,000 in 2003 and have two children attending college. They ordinarily would owe income tax of \$330 and would qualify for an EIC of \$2,041. However, during 2003 they made contributions of \$1,000 to Meg's retirement plan at work through pre-tax salary deductions. This reduces their taxable income to \$24,000, and lowers their income tax by \$100 to \$230. Since only their taxable earned income is considered in calculating the EIC, they will qualify for a higher EIC of \$2,252, an increase of \$211. And, they can take the Saver's Tax Credit, worth up to 50 percent of their contribution amount, or as much as \$500. The Saver's Tax Credit eliminates their \$230 income tax, and they still receive their EIC of \$2,252. Overall, by making the \$1,000 contribution to Meg's retirement account and taking the Saver's Tax Credit, the couple gets a tax benefit of \$541. (Their original income tax amount was reduced by \$100 and then the remaining \$230 was eliminated, for a total tax reduction of \$330. In addition, by reducing their taxable income, they were able to claim an EIC that was \$211 higher than it would have been had they not made the retirement plan contribution: $\$330 + \$211 = \$541$.)

Who Is Eligible to Claim the Saver's Tax Credit?

The credit may be claimed by taxpayers who:

- are age 18 or older,
- are not full-time students,
- are not claimed as a dependent on someone else's return; and
- have adjusted gross income in 2003 no higher than these amounts:
 - \$50,000 if married filing jointly
 - \$37,000 if filing as head of household
 - \$25,000 if filing single, or married filing separately

What Retirement Contributions Qualify for the Saver's Tax Credit?

Contributions workers elect to make through salary reduction to a variety of employer-administered retirement plans are eligible for the credit, as are contributions to both traditional and Roth Individual Retirement Accounts (IRAs). Salary reduction contributions made to the following types of plans are eligible:

- a 401(k) plan, including a SIMPLE 401(k)
- a section 403(b) annuity
- an eligible deferred compensation plan of a state or local government (a "governmental 457 plan")
- a SIMPLE IRA plan
- a salary reduction SEP (simplified employee pension)

Individuals entitled to deduct IRA contributions may still do so and also claim the Saver's Tax Credit. Voluntary after-tax contributions to a qualified retirement plan or 403(b) annuity also qualify for the Saver's Tax Credit.

How Is the Amount of the Saver's Tax Credit Figured?

The credit can range from 10 percent to 50 percent of the worker's contribution to retirement, based upon the worker's adjusted gross income for the tax year. In the example of Randy and Meg above, their taxable income of \$24,000 as married joint filers qualifies them for a credit worth 50 percent of their \$1,000 contribution.

How do Workers Claim the Saver's Tax Credit?

Workers must complete IRS Form 8880, "Credit for Qualified Retirement Savings Contributions," enter the amount of the credit on Form 1040 or 1040A, and attach Form 8880 to their tax return.

Form 8880 may be downloaded from the IRS website at: www.irs.gov/formspubs. For additional information, see *IRS Announcement 2001-106, pg. 416, "Saver's Tax Credit for Contributions by Individuals to Employer Retirement Plans and IRAs"* at: www.irs.gov/pub/irs-irbs/irb01-44.pdf.

2003 Adjusted Gross Income

Married filing jointly	Head of household	All other filers	Credit
\$0 - \$30,000	\$0 - \$22,500	\$0 - \$15,000	50% of contribution
\$30,001 - \$32,500	\$22,501 - \$24,370	\$15,001 - \$16,250	20% of contribution
\$32,501 - \$50,000	\$24,376 - \$37,500	\$16,251 - \$25,000	10% of contribution
Over \$50,000	Over \$37,500	Over \$25,000	Credit not available

EIC Benefits for Tax Year 2003 at Various Income Levels

This is not a tax table. Do not use this table to complete income tax returns.

2003 household income	Workers not raising a child		Workers raising one child		Workers raising two or more children		
	Is Worker Married?.	Not Married	Married	Not Married	Married	Not Married	Married
\$ 500		\$40	\$40	\$179	\$179	\$210	\$210
1,000		78	78	349	349	410	410
1,500		117	117	519	519	610	610
2,000		155	155	689	689	810	810
2,500		193	193	859	859	1,010	1,010
3,000		231	231	1,029	1,029	1,210	1,210
3,500		270	270	1,199	1,199	1,410	1,410
4,000		308	308	1,369	1,369	1,610	1,610
4,500		346	346	1,539	1,539	1,810	1,810
5,000		382	382	1,709	1,709	2,010	2,010
5,500		382	382	1,879	1,879	2,210	2,210
6,000		382	382	2,049	2,049	2,410	2,410
6,500		347	382	2,219	2,219	2,610	2,610
7,000		322	382	2,389	2,389	2,810	2,810
7,500		283	360	2,547	2,547	3,010	3,010
8,000		245	322	2,547	2,547	3,210	3,210
8,500		207	283	2,547	2,547	3,410	3,410
9,000		169	245	2,547	2,547	3,610	3,610
9,500		130	207	2,547	2,547	3,810	3,810
10,000		92	169	2,547	2,547	4,010	4,010
10,500		54	130	2,547	2,547	4,204	4,204
11,000		16	92	2,547	2,547	4,204	4,204
11,500		0	54	2,547	2,547	4,204	4,204
12,000		0	16	2,547	2,547	4,204	4,204
12,500		0	0	2,547	2,547	4,204	4,204
13,000		0	0	2,547	2,547	4,204	4,204
13,500		0	0	2,547	2,547	4,204	4,204
14,000		0	0	2,499	2,547	4,142	4,204
14,500		0	0	2,420	2,547	4,037	4,204
15,000		0	0	2,340	2,499	3,931	4,142
15,500		0	0	2,260	2,420	3,826	4,037
16,000		0	0	2,180	2,340	3,721	3,931
16,500		0	0	2,100	2,260	3,615	3,826
17,000		0	0	2,020	2,180	3,510	3,721
17,500		0	0	1,940	2,100	3,405	3,615
18,000		0	0	1,860	2,020	3,299	3,510
18,500		0	0	1,780	1,940	3,194	3,405
19,000		0	0	1,700	1,860	3,089	3,299
19,500		0	0	1,621	1,780	2,984	3,194
20,000		0	0	1,541	1,700	2,878	3,089
20,500		0	0	1,461	1,621	2,773	2,984
21,000		0	0	1,381	1,541	2,668	2,878
21,500		0	0	1,301	1,461	2,562	2,773
22,000		0	0	1,221	1,381	2,457	2,668
23,000		0	0	1,061	1,221	2,246	2,457
24,000		0	0	901	1,061	2,036	2,246
25,000		0	0	742	901	1,825	2,036
26,000		0	0	582	742	1,615	1,825
27,000		0	0	422	582	1,404	1,615
28,000		0	0	262	422	1,193	1,404
29,000		0	0	102	262	983	1,193
30,000		0	0	0	102	772	983
31,000		0	0	0	0	562	772
32,000		0	0	0	0	351	562
33,000		0	0	0	0	140	351
34,000		0	0	0	0	0	140

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