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Should the EITC for Workers Without Children Be Abolished, Maintained, or Expanded?

by Robert Greenstein

Alongside the substantial Earned Income Tax Credit for low-income working families with children is a small EITC for workers between the ages of 25 and 64 who are not raising minor children. The EITC for families that do have children provides an average credit of more than $1,900 and covers families with incomes up to $27,400 or $31,200, depending on the number of children in the family. By contrast, the EITC for workers *without* children provides an average credit of approximately $200 and ends when income reaches $10,400.

Some 98 percent of overall EITC benefits goes to families with children, with two percent going to working individuals and married couples who are not raising minor children. The cost of this small EITC for workers without children amounts to about $700 million a year.

On several occasions in recent years — and particularly in 1995 and 1996 — proposals to abolish this credit have emerged. Such proposals were advanced in the mid-1990s as a way to help eliminate the budget deficit, while also making room for various tax cuts. More recently, elimination of this credit has been suggested on a few occasions as an offset to help finance tax cuts or entitlement expansions, although no legislation to this effect has been moved.

Since this small credit is never larger than the employee share of the payroll tax — it offsets this payroll tax for only the first $4,600 in earnings — abolishing it would leave the overall tax burdens of these workers higher. In other words, it would raise their taxes. As explained below, this group of low-income workers already pays a surprisingly high percentage of its income in federal taxes. More than three million of the nation's poor workers would be adversely affected by elimination of this credit. Many of them would be pushed deeper into poverty.

Rather than abolishing this part of the EITC, or maintaining it in its current form, Congress may wish to enlarge it. These workers face high federal tax burdens. They also are ineligible for most forms of government assistance despite the fact that a large majority of them live in poverty. If any group of workers needs a tax cut, it is this group. In addition, these workers might be induced to work more by a somewhat more substantial EITC.

Background

The EITC for childless workers is a tax credit for poor workers between the ages of 25 and 64 who do not live with minor children. In 2000, the EITC for which these workers can qualify equals 7.65 percent of their first $4,610 in earnings, resulting in a maximum credit of $353. The credit begins to phase out at a 7.65 percent rate once a worker's income surpasses $5,770. The credit falls to zero when income reaches $10,380.

In tax year 1998, some 3.3 million filers received this EITC. The average credit they received was $212.

This modest EITC was established for these workers in 1993, in part because their federal tax burdens had escalated sharply since 1980 as a result of a series of regressive payroll and excise tax increases and in part because the 1993 budget package contained a further tax increase of this nature. A Congressional Budget Office analysis found that between 1980 and 1993, the average federal tax burden of the poorest fifth of non-elderly households climbed *38 percent*, dwarfing the increase in tax burdens borne during this period by any other group of households in any income category (see Table 2). By 1993, the percentage of income that the poorest fifth of non-elderly households without children was paying in federal taxes was double the percentage of income that the poorest fifth of families with children paid and more than five times the percentage that the poorest fifth of elderly households paid.

The sharp increase in the tax burdens these households bear resulted primarily from increases in Social Security, gasoline, and other excise taxes. For working families with children that have low incomes, those regressive tax increases generally were offset through EITC expansions. By contrast, for poor workers without children, no offsetting actions were taken before 1993, when the small EITC for these workers was created.

In addition to offsetting a portion of these various tax increases, the establishment of the EITC for poor childless workers also partially addressed a piece of unfinished business from the 1986 Tax Reform Act. One of that Act's goals, often espoused by President Ronald Reagan, was to eliminate federal income taxes on workers below the poverty line so they would not be taxed deeper into poverty. The 1986 Act accomplished this goal for all tax filers *except* non-elderly single individuals. Prior to extension of the EITC to these workers, a single non-elderly worker continued to owe federal income tax when his or her income was well below the poverty line. The EITC raised the income level at which these workers begin to owe income tax, but that level still remains below the poverty line.

Effects of Abolishing the Credit

Abolishing this small EITC would result in a tax increase for some of the nation's poorest workers. As just noted, single workers are the only group in the United States who begin to owe federal income tax before their income reaches the poverty line; the federal income tax code taxes them somewhat more deeply into poverty. Abolishing their EITC would make their tax burdens larger, pushing them farther below the poverty line.

The poverty line for a single non-elderly individual is projected to be $8,884 in 2000. A single individual begins to owe federal income tax when his or her earnings equal $8,276. A worker with earnings equal to the poverty line must pay $138 in federal income tax in 2000 *after* the EITC is taken into account, along with $1,359 in payroll taxes (including the employer share). This worker thus pays a total of $1,497 in federal income and payroll taxes. These taxes push the worker below the poverty line.

Without the small EITC that these poor single workers can receive, they would begin owing federal income tax when their income surpassed $7,200. If this credit is abolished, workers with incomes equal to the poverty line will see their combined income and payroll tax burden rise to more than $1,600.

Table 1

Earned Income Credit Claims for Tax Year 1998 by Workers Without a Qualifying Child

	Number	Amount
Alabama	52,708	$11,339,152
Alaska	6,130	$1,106,371
Arizona	53,037	$11,324,187
Arkansas	33,249	$6,972,567
California	416,674	$92,062,983
Colorado	49,542	$10,141,844
Connecticut	30,996	$6,492,745
Delaware	7,971	$1,720,147
District of Columbia	8,880	$1,965,044
Florida	238,272	$51,496,620
Georgia	89,002	$19,138,319
Hawaii	15,732	$3,229,647
Idaho	13,836	$2,941,199
Illinois	125,174	$26,334,843
Indiana	63,802	$12,921,403
Iowa	29,099	$5,805,602
Kansas	24,325	$4,929,858
Kentucky	54,940	$11,163,708
Louisiana	55,363	$12,157,286
Maine	17,659	$3,566,634
Maryland	52,077	$11,094,460
Massachusetts	64,601	$13,490,650
Michigan	100,654	$21,055,629
Minnesota	45,197	$9,099,430
Mississippi	33,439	$7,245,540
Missouri	63,591	$13,029,084
Montana	14,307	$2,933,185
Nebraska	16,664	$3,296,671
Nevada	22,582	$4,632,442
New Hampshire	12,068	$2,454,421
New Jersey	77,276	$16,713,890
New Mexico	33,030	$6,863,751
New York	257,950	$57,336,395
North Carolina	91,591	$19,415,926
North Dakota	7,783	$1,531,679
Ohio	126,082	$25,943,477
Oklahoma	46,138	$9,521,449
Oregon	41,629	$8,595,864
Pennsylvania	138,204	$28,257,872
Rhode Island	12,540	$2,515,413
South Carolina	52,056	$10,907,720
South Dakota	9,114	$1,793,845
Tennessee	77,204	$15,856,642
Texas	245,443	$52,519,732
Utah	16,260	$3,441,095
Vermont	8,773	$1,782,808
Virginia	74,352	$15,561,070
Washington	62,516	$12,898,879
West Virginia	28,120	$5,636,392
Wisconsin	48,848	$9,845,710
Wyoming	6,972	$1,367,495
National	3,273,452	$693,448,773

Source: IRS Supplemental Earned Income Report January 6, 2000

Table 2

Changes in Federal Tax Burdens, 1980-1993

Household Category	Change in the Percentage of Income Consumed by Federal Taxes
Non-elderly households without children	
poorest fifth	+38%
middle fifth	5
top fifth	-3
All households	
poorest fifth	4%
middle fifth	-2
top fifth	-3

Source: Congressional Budget Office data published in House Committee on Ways and Means, *1992 Green Book*, pp. 1526-7.

This clearly would constitute a tax increase. The EITC these worker can receive never exceeds 7.65 percent of their wages, the amount withheld from their paychecks for the employee share of payroll taxes. Without this EITC, these workers would receive no offset to their payroll tax burdens. Elimination of this credit consequently would result in a tax increase even for workers too poor to owe any federal income tax. With none of their payroll taxes offset, their net tax burden would rise.

Terminating the EITC for these workers would raise the tax burdens of the more than three million very poor workers who currently receive it. If such a step were taken, and some of the tax-cut measures the House or Senate have passed this year were enacted at the same time, some of the nation's poorest workers would face a tax increase while many of the nation's wealthiest individuals received lavish tax cuts.

An Alternative Approach

An alternative course to abolishing this credit or retaining it in its current form would be to enlarge it somewhat. This could be done, for example, by increasing this credit from 7.65 percent of the first $4,610 in wages to 15.3 percent of a somewhat higher level of wages, as well as by not beginning to phase the credit down until a worker's income reaches a somewhat higher level than $5,770, the level at which the credit now begins phasing down. (The 15.3 percent figure is the amount needed to offset the full amount of the payroll tax, including the employer share. Most economists believe that both the employer and employee shares of the payroll tax are borne by workers in the form of lower wages.) Expanding the credit also might serve two other beneficial purposes — it might draw more single workers into the labor force, and it should raise the incomes of some poor non-custodial fathers, thereby increasing their ability to pay child support.

Recent research has found that the large expansions since 1986 in the EITC for families with children have resulted in a substantial increase in the proportion of single mothers that are employed. In fact, some research has found that the EITC expansions have had an even-larger effect in increasing employment among single mothers than changes in welfare policy. Other research has found the welfare policy changes to have had the largest effect, with the EITC expansions a strong second. In either case, the employment-promoting effects of the expansions in the EITC for families with children appear to be large.[1]

Employment remains relatively low among some groups of single men. For example, in 1999, some 74.5 percent of African-American men aged 25-34 who do not reside with children were employed (as compared to an 86 percent employment rate among all men in this age group). In other words, one-fourth of African-American men in this age group were not employed. If enlarging the EITC for workers not raising minor children induced an increase in employment among this group, as increases in the EITC for families with children have done among single mothers — expanding the EITC for childless workers would be particularly beneficial.

Even with EITC, Childless Workers Face Large Tax Burdens

EITC for Poor Workers Without Children Accounts for a Tiny Fraction of EITC Errors and is Not Rising in Cost

In 1997, the Internal Revenue Service issued the results of a study of errors in the Earned Income Tax Credit. The study found that errors in the EITC for workers without children cause little revenue loss. The study showed that errors in this component of the EITC account for less than two percent of EITC overpayments and that the error rate for this component of the credit is lower than the error rate for the EITC that families with children receive and about equal to the average error rate for the income tax code as a whole.*

Furthermore, budget data from the Treasury Department and the Office of Management and Budget also indicate that the EITC for childless workers is growing little in cost. The Treasury projects that the cost of the EITC for childless workers will actually decline between 1999 and 2001 and not return to the 1999 level until 2003. In fiscal year 1999, the EITC for childless workers cost $684 million. It is projected to cost $652 million in 2001 and $681 million in 2003. Between 1999 and 2005, the annual average rate of cost growth is projected to be less than one percent. That is less than one-third the projected inflation rate and less than one-fifth the rate at which the U.S. economy is expected to grow.

* See Robert Greenstein, "The Earned Income Tax Credit and Error Rates," Center on Budget and Policy Priorities, February 25, 1998.

Another reason to expand the EITC for poor workers not raising minor children is that even with the current EITC, these workers pay a strikingly high percentage of their small incomes in federal taxes. As noted, if any workers need a tax cut, these workers do.

The Congressional Budget Office has estimated that the poorest fifth of non-elderly individuals who live alone paid an average of 17.1 percent of their income in federal taxes for 1999. The poorest fifth of non-elderly couples without children, on average, paid an estimated 11 percent of income in federal taxes.[2] Low-income workers not raising minor children were essentially untouched by the tax cuts enacted in 1997.

These figures far surpass the percentages of income that poor elderly individuals and poor families with children pay. In fact, the 17.1 percent-of-income that the poorest fifth of non-elderly individuals living alone pay in federal taxes is nearly as large as the average tax burden that the middle fifth of families with children bear.

These Workers Receive Few Other Benefits

Moreover, workers who qualify for this modest credit can receive few if any other government benefits. They generally are ineligible for means-tested cash and medical assistance funded in whole or in part by the federal government; such assistance is limited to families with children, the elderly, and the disabled. This also is true for most housing assistance. The ability of these individuals to receive food stamps is restricted, as well.

Conclusion

With budget surpluses growing, Congress is considering an array of tax cuts. Enlarging the small EITC for very poor workers not raising minor children, a measure that would have a very low cost and would benefit some of the nation's poorest workers, merits consideration. It would represent a far sounder policy course that abolishing this small tax credit and taxing several million low-income workers deeper into poverty.

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1. See Bruce D. Meyer and Dan T. Rosenbaum, "Welfare, the Earned Income Tax Credit, and the Labor Supply of Single Mothers," National Bureau of Economic Research, Working Paper 7363, September 1999; Meyer and Rosenbaum, "Making Single Mothers Work: Recent Tax and Welfare Policy and its Effects, December 1999; David T. Ellwood, "The Impact of the Earned Income Tax Credit and Social Policy Reforms on Work, Marriage, and Living Arrangements," November 1999; and Robert Greenstein and Isaac Shapiro, "New Research Findings on the Effects of the Earned Income Tax Credit," Center on Budget and Policy Priorities, March 1998.

2. CBO Memorandum, "Estimates of Federal Tax Liabilities for Individuals and Families by income Category and Family Type for 1995 and 1999," May 1998, pp. 28-9. In accordance with standard economic analysis, the figures in the CBO analysis, as well as in the CBO data in Table 2, include both the employer and the employee share of the payroll tax.