Center on Budget and Policy Priorities

820 First Street NE, Suite 510
Washington, DC 20002

Tel: 202-408-1080
Fax: 202-408-1056

center@cbpp.org
www.cbpp.org

Special Series: **Economic Recovery Watch**

February 16, 2010

FAILURE TO EXTEND IMPROVEMENTS IN CHILD TAX CREDIT WOULD HARM MILLIONS OF LOW-INCOME WORKING FAMILIES

By Arloc Sherman, Avi Feller, and Chuck Marr

The American Recovery and Reinvestment Act of 2009 (ARRA) expanded the child tax credit to reach many low-income working families who previously were excluded from it and boosted the credit for many more such families who were receiving only a fraction of the full credit. This action helped millions of children whose parents are child care workers, preschool staff, home health aides, cashiers at retail stores, waiters or waitresses, dishwashers, grounds maintenance workers, people who clean offices or homes, and others who work for very low wages.

President Obama's fiscal year 2011 budget, as well as legislation that Senate Finance Committee chairman Max Baucus introduced last year, would make this change permanent along with the child-tax-credit expansion that Congress enacted in 2001 and many other tax cuts it enacted in 2001 and 2003. If Congress fails to extend the 2009 improvements, most likely as part of expected legislation to make the so-called "middle class tax cuts" permanent, millions of low-income working families with children will lose much or all of their child tax credit, and many will fall into — or deeper into — poverty. Estimates from the Urban Institute-Brookings Institution Tax Policy Center show that if Congress extends the 2001 and 2003 tax cuts without also extending the 2009 child tax credit improvements:

- Low-income working families with 7.6 million children will lose all of their child tax credit.
- Low-income working families with an additional 10.5 million children will continue to receive a credit but have their credit cut, in many cases by large amounts.
- The families that stand to lose the most would be those with incomes between $12,850 and $16,333, including many families where a parent works full time at the minimum wage. Families with incomes above $10,000 would experience 80 percent of the losses.

In addition, an analysis of Census data shows that:

- If Congress does not extend the 2009 child tax credit improvements, 600,000 children will fall into poverty as the loss of some or all of the credit pushes their families' incomes below the poverty line. An additional 4 million children who already are poor will fall deeper into poverty.
- The parents who stand to lose include large numbers of preschool teachers, nurses' aides and other low-wage health care workers, cooks and wait staff, and custodial staff.

Background

Congress created the child tax credit in 1997 to help families meet the costs of raising children and then expanded it in 2001 and 2009.[1] The full credit is worth $1,000 per child. The credit is partially refundable, which means that some (but not all) low-income families who do not incur a federal income tax liability can receive the credit — usually a partial credit.

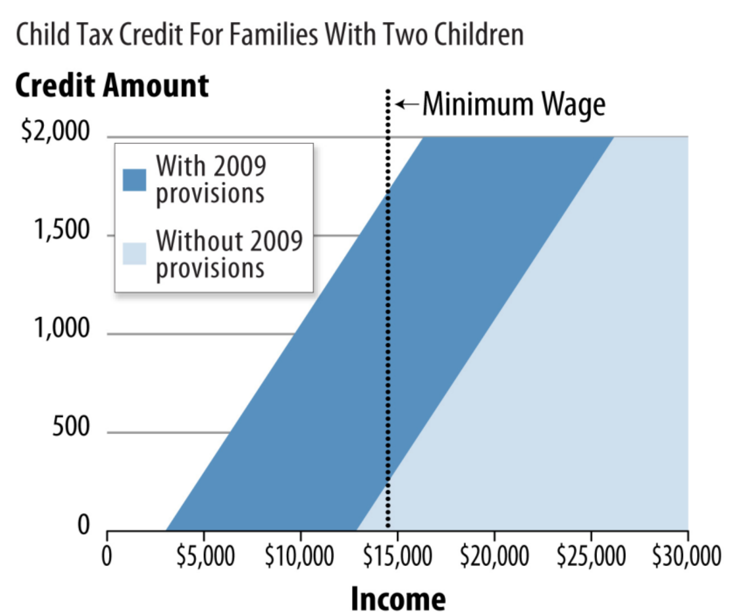
Under the 2001 tax-cut law, which made the child credit partially refundable, low-income working families received no child credit on their first $10,000 of wages and then received a credit of 15 cents for every dollar they earned above that threshold until their credit equaled the full $1,000 per child. A family with two children would need earnings of $23,333 before it could qualify for the full credit. This $10,000 'zero-credit threshold" was adjusted for inflation; by 2007, families needed to earn close to $12,000 before qualifying for any child tax credit.

In 2008, Congress lowered the zero-credit threshold to $8,500 for that year. This reduced to $21,993 the amount a family with two children needed to earn to qualify for the full credit. In 2009, ARRA established the parameters for the credit that are now in effect: low-income families receive no credit for their first *$3,000* of wages and receive a credit of 15 cents for each dollar of wages above that level. A family with two children now is able to receive the full credit when its earnings reach $16,333.

Congress must act this year to deal with numerous tax cuts that are slated to expire at the end of 2010. The fate of the 2009 child tax credit improvement is uncertain.

- If Congress extends the 2009 child credit provisions as part of broader proposals to extend "middle-class" tax cuts, a family with two children in which a parent works full time at the minimum wage will continue to be eligible for a child credit of $1,725 in 2011.
- But if Congress extends the 2001 child credit provisions *without* the 2009 child credit provisions, this minimum-wage family will have its credit reduced by $1,477 — or 86 percent — to $248 in 2011. Meanwhile, a family with two children that makes $100,000 will continue to receive a full child credit of $2,000.

FIGURE 1:
Allowing 2009 Child Credit Improvements to Expire Would Harm Working Families



[1] The tax credit also was expanded for one year in 2008.

TABLE 1: How Much Will a Family with Two Children Receive in 2011 from the Child Tax Credit?			
Earnings	**Under today's rules (i.e., the provisions enacted in 2009)**	**Under the 2008 parameters**	**If the 2001 law is extended *without* extending the child tax credit provisions enacted in 2009**
$6,000	$450	$0	$0
$12,000	$1,350	$525	$0
$18,000	$2,000	$1,425	$773

Note: Under the provisions currently in effect, there are no child tax credit benefits for the first $3,000 of wages. Under the 2008 parameters, the zero-credit threshold is $8,500; if the 2001 tax cuts are extended but the subsequent improvements in the child tax credit are jettisoned, the zero-credit threshold will rise to $12,850 in 2011.

A return to the 2008 child tax credit parameters, under which no credit was provided for a worker's first $8,500 of wages, also would substantially shrink the child tax credit for millions of working-poor families.

- The minimum-wage family cited above would see its child tax credit reduced by $825 (or 48 percent), to $900.
- About 14 million low-income children would have their child credit eliminated or receive a smaller credit than if Congress maintains the current child credit parameters.

Current Child Credit Rules Promote Work

By lowering the amount of wages that a family must earn before it qualifies for any child tax credit (and before the credit begins to increase for each additional dollar a family earns), the ARRA child credit improvements give parents who are out of work a more powerful incentive to look for and take offers of even very low-paying jobs and part-time jobs, if that is all they can find. These improvements also give poor parents who are already employed an incentive to try to secure more hours of work and raise their earnings.

Consider a parent who is out of work and has two children. If, part-way through the year, she is able to take a job and earn something over $3,000, she will receive a partial child credit, which she would *not* receive if she remained jobless. And because the child credit increases as her earnings rise, she has an incentive to stay employed and to increase her earnings.

Failure to Extend Current Rules Would Shrink or Eliminate Credit for Millions

If Congress extends many or all of the 2001 and 2003 tax cuts but fails to extend the current child tax credit rules, families that earn less than $12,850 would be entirely shut out of the credit, and families earning modestly more than that would experience deep cuts in the credit. Tax Policy Center data show that 18.1 million children would have their child credits reduced — 7.6 million children would lose the credit entirely and nearly 10.5 million additional children would receive a smaller credit.[2] (See Table 2 for state-by-state estimates.)

[2] Source: TPC table T10-0009. Figures are based on IRS rules for 2009, when the threshold in the absence of ARRA would have been $12,550.

In addition, 600,000 children would be pushed into poverty because the loss of part or all of the credit would lower their families' incomes below the poverty line. An additional 4 million children who already are poor would become poorer.

The impact on low-income families would also be sharp if Congress extends the 2008 child tax credit rules rather than the current ones. Under that approach, low-income families would receive no child credit for their first $8,500 in wages.

- Under this option, about 14 million children would see their child tax credit reduced or eliminated, relative to the credit they would receive if the current rules are made permanent, as President Obama and Chairman Baucus have proposed.[3]

- Some 600,000 children would be pushed into poverty, and 4 million already poor children would become poorer.

Which Families Would Have Their Tax Credit Cut?

Some people may mistakenly assume that only people with incomes relatively close to $3,000 (the current threshold to qualify for the child credit) would be affected if the threshold were to rise. In reality, because the credit phases in slowly above this threshold — as noted, the full credit of $1,000 per child does not kick in until a family with two children earns more than $16,333 — changing the threshold would affect families at much higher income levels. For example:

- A preschool teacher who earns $18,000 and has two children would see her child credit cut by over $1,200 if Congress extends the 2001 and 2003 tax cuts but fails to extend the current child tax credit rules. (Her credit would be cut by $575 if Congress restores the 2008 child credit parameters instead.)

- Families with earnings close to $3,000, by contrast, would lose much smaller amounts. A family with just $3,100 in earnings receives a credit of only $15 under the current rules and would lose that amount. (This family's credit equals 15 percent of the amount — $100 — by which its earnings exceed $3,000.)

- Indeed, the Tax Policy Center's analysis shows that families with incomes above $10,000 would bear 80 percent of the tax credit losses if Congress fails to extend the current child credit rules.[4] Families with two children would face a cut in their child tax credit until their earnings reached $26,180. Families with three children would have their credit cut unless their earnings exceeded $32,850.[5]

- The parents in most families whose child tax credit would be reduced work throughout the year. Census data show that nearly 70 percent of the children whose credit would be cut live in

---

[3] For a discussion of the Administration's proposal, which is reflected in its FY 2011 budget, see the Treasury Department's "Green Book," available at http://www.treas.gov/offices/tax-policy/library/greenbk10.pdf. The Green Book estimates the cost of making permanent the Child Tax Credit provision enacted as part of ARRA at about $9 billion a year.

[4] Source: TPC Table T10-0007.

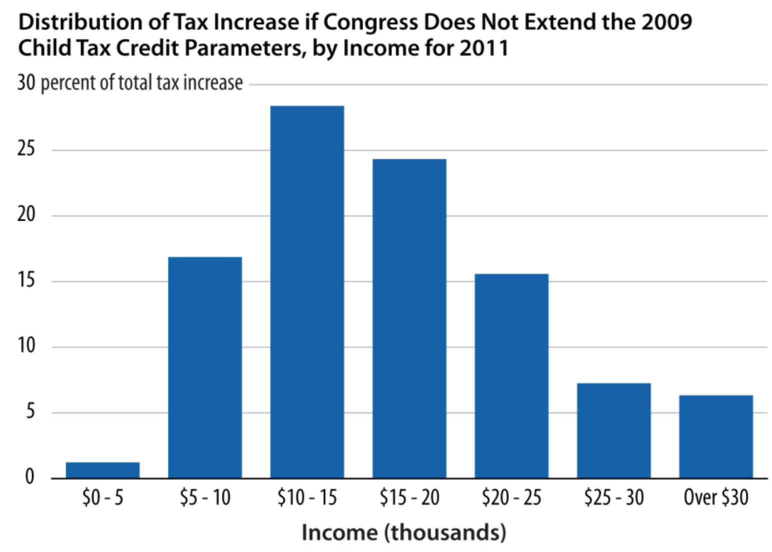
[5] These are the earnings levels a family will have to attain before it can receive the full credit if the zero-credit threshold is raised to $12,800, since a family's credit cannot exceed 15 percent of the amount by which its earnings exceed that threshold.

a family where a person is employed throughout the year. Most of the remaining families work for more than half of the year.

- Some 2.5 million children — one in every seven children whose tax credit would be reduced — live in a family in which a parent or a child has a disability. These parents often struggle to maintain their jobs and meet the additional health and other expenses they incur due to the disability. Also, the disability often restricts the number of hours they can work.

FIGURE 2:

Families with Incomes Above $10,000 Would Absorb Majority of Tax Increase if Current Rules Not Extended



Source: CBPP Calculations based on Census and TPC data

What Types of Low-Wage Occupations Would Be Affected?

According to Census data, many of the parents who would face large cuts in their child tax credit if Congress fails to extend the current rules are employed in low-paying jobs that are important to the economy and local communities:

- 330,000 of these parents provide child care, serve as teaching assistants, or teach preschool or kindergarten.

- 420,000 are nursing home workers, home health aides, personal care assistants, medical assistants, or other low-wage health care workers.

- 630,000 clean or maintain the grounds of homes, office buildings, schools, or other institutions.

- 450,000 are cashiers in grocery stores or other businesses.

- 590,000 are cooks (or assist cooks with food preparation), waiters or waitresses, cafeteria workers, or dishwashers.

- 650,000 are construction workers, carpenters, electricians, or painters.

- 210,000 work in the agricultural industry with crops or farm animals.

TABLE 2: Extending 2001 and 2003 Tax Cuts Without Extending Current Child Credit Rules Would Affect Large Numbers of Parents in Every State		
Tax year 2011		
	Number of Children Whose Credit Would Be Reduced or Eliminated	**Margin of Error**
U.S. Total	**18,100,000**	
Alabama	278,000	±37,000
Alaska	42,000	±6,000
Arizona	484,000	±59,000
Arkansas	230,000	±27,000
California	2,495,000	±124,000
Colorado	270,000	±41,000
Connecticut	143,000	±25,000
Delaware	40,000	±7,000
District of Columbia	32,000	±6,000
Florida	1,037,000	±79,000
Georgia	608,000	±60,000
Hawaii	62,000	±9,000
Idaho	116,000	±14,000
Illinois	732,000	±65,000
Indiana	361,000	±45,000
Iowa	170,000	±25,000
Kansas	161,000	±25,000
Kentucky	291,000	±39,000
Louisiana	333,000	±41,000
Maine	55,000	±10,000
Maryland	167,000	±31,000
Massachusetts	252,000	±36,000
Michigan	584,000	±56,000
Minnesota	202,000	±32,000
Mississippi	205,000	±26,000
Missouri	354,000	±44,000
Montana	63,000	±8,000
Nebraska	94,000	±14,000
Nevada	152,000	±23,000
New Hampshire	42,000	±8,000
New Jersey	307,000	±41,000
New Mexico	169,000	±22,000
New York	1,072,000	±77,000
North Carolina	578,000	±58,000
North Dakota	32,000	±5,000
Ohio	601,000	±56,000
Oklahoma	236,000	±32,000

Oregon	239,000	±35,000
Pennsylvania	576,000	±55,000
Rhode Island	50,000	±9,000
South Carolina	282,000	±39,000
South Dakota	38,000	±6,000
Tennessee	423,000	±48,000
Texas	2,111,000	±115,000
Utah	203,000	±25,000
Vermont	28,000	±5,000
Virginia	295,000	±40,000
Washington	333,000	±45,000
West Virginia	102,000	±14,000
Wisconsin	294,000	±39,000
Wyoming	29,000	±5,000

Source: Tax Policy Center (Table T10-0009) national estimates, allocated by state by CBPP using Current Population Survey data.