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How Much Would a State Earned Income Tax Credit Cost in Fiscal Year 2021?

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Twenty-nine states plus the District of Columbia and Puerto Rico have enacted earned income tax credits (EITCs) to supplement the federal EITC, one of the nation’s most effective tools for boosting the incomes of families paid low wages. Federal and state EITCs help these families meet basic needs and pay for things that allow them to keep working, such as child care and transportation. This income boost helps millions of people struggling to get by on low incomes meet basic needs. The federal EITC kept 5.6 million people — over half of them children — out of poverty in 2018, and helped many with somewhat higher incomes make ends meet.

The EITC also has lasting benefits for children. Young children in low-income households that get an income boost from the state or federal EITC tend to do better and go further in school, reducing the disadvantages associated with exposure to poverty.¹ The EITC may play a particularly important role in helping children of color improve their math achievement, complete high school, and enroll in college, the research suggests.²

State EITCs are a common-sense way to amplify the positive impact of the federal credit. They help working families keep more of what they earn by reducing the substantial state and local taxes they pay, leaving them with more to cover basic expenses and give their children a better start in life.

¹ Chuck Marr *et al.*, “EITC and Child Tax Credit Promote Work, Reduce Poverty, and Support Children’s Development, Research Finds,” Center on Budget and Policy Priorities, updated October 1, 2015, <https://www.cbpp.org/research/federal-tax/eitc-and-child-tax-credit-promote-work-reduce-poverty-and-support-childrens>; Greg J. Duncan, Pamela A. Morris, and Chris Rodrigues, “Does Money Really Matter? Estimating Impacts of Family Income on Young Children’s Achievement with Data from Random-Assignment Experiments,” *Developmental Psychology*, June 2011, pp. 1263–1279.

² Michelle Maxfield, “The Effects of the Earned Income Tax Credit on Child Achievement and Long-Term Educational Attainment,” Michigan State University Job Market Paper, November 14, 2013, <https://www.msu.edu/~maxfiel7/20131114%20Maxfield%20EITC%20Child%20Education.pdf>; Katherine Michelmore, “The Effect of Income on Educational Attainment: Evidence from State Earned Income Tax Credit Expansions,” November 2013, <https://ssrn.com/abstract=2356444>; Gordon Dahl and Lance Lochner, “The Impact of Family Income on Child Achievement: Evidence from the Earned Income Tax Credit,” *American Economic Review*, August 2012, pp. 1927-1956.

Policymakers considering a state-level EITC can estimate its cost using the simple three-step process outlined below.

Data Sources

CBPP's methodology for estimating the cost of a state EITC employs two data sources. First, we use Internal Revenue Service (IRS) statistics on the value of all federal EITC claims filed by residents of each state to determine the state's share of total U.S. EITC claims. The most recent full-year data, shown in the second column of Table 1, are for claims made for the 2017 tax year.³

Second, projections by the congressional Joint Committee on Taxation (JCT) of the future cost of the federal EITC provide a base for estimating the cost of a state EITC. For fiscal year 2021, the JCT estimates that the federal EITC will cost over \$73.1 billion.⁴

The federal EITC is refundable, meaning that workers get the full value of the credit they earned, even if it exceeds what they owe in federal income taxes; EITC refunds help offset substantial other taxes that low-income workers pay, like Social Security and Medicare payroll taxes and the federal gas tax. Low- and moderate-income households in most states pay more as a share of their income in state and local taxes than do upper-income families.⁵ Most state EITCs are refundable as well, so they both reduce or eliminate state and local income taxes and help offset low-income workers' sales taxes, property taxes, and other state and local taxes and fees.

Three Steps to Estimating the Cost of a State EITC

Step 1: Estimate the total value of federal EITC claims in a given state for a future fiscal year. To estimate the total value of the federal EITC in a given state in a future fiscal year, we first use the IRS data on EITC claims to divide the value of EITC claims in that state by the value of all U.S. EITC claims. This percentage is the share of the federal EITC cost attributable to that state in the base year (2017). Then, to estimate the cost of the federal EITC in the state for a future year, we apply that percentage to JCT's projected total cost of the federal EITC for the chosen year.

For example, for tax year 2017, Alabama EITC claims were \$1.38 billion, or 2.11 percent of the nationwide total. Assuming that Alabama's share of federal EITC claims remains constant, Alabama's federal EITC claims in fiscal year 2021 would be 2.11 percent of \$73.1 billion, or \$1.542 billion, as the fourth column of Table 1 shows.

Step 2: Multiply the expected value of the state's federal EITC claims by the percentage of the federal credit at which the state credit will be set. Most states' EITCs are a set percentage of

³ All but a tiny fraction of federal EITCs for a given year are claimed and paid when taxes are filed in January through April of the following year. As a result, nearly all of the federal costs for tax year 2017 EITCs were incurred in federal fiscal year 2018, which ended September 30, 2018. Similarly, in most states the cost of tax year 2019 claims will fall in the state fiscal year that ends in 2020.

⁴ Estimates of the future cost of the federal EITC come from JCT's "Estimates of Federal Tax Expenditures for Fiscal Years 2019-2023." The JCT estimate of the federal EITC's cost includes both the tax expenditure (non-refundable) and outlay (refundable) portions.

⁵ Institute on Taxation and Economic Policy, "Who Pays, 6th Edition," <https://itep.org/whopays/>.

the federal credit. This percentage for refundable credits ranges from 3 percent to 40 percent, depending on the state.⁶ To estimate the cost of a state EITC, multiply the federal EITC cost for the state, as determined in Step 1, by the percentage at which the state EITC is to be set. This calculation yields an estimate of what the state credit would cost in a given fiscal year if everyone who received the federal credit also received the state credit.

Step 3: Adjust the estimate for the fact that not all federal EITC claimants will claim the state credit. In practice, a substantial portion of those who receive the federal EITC fail to claim state EITCs. This is especially true in the first few years after a state enacts a credit, when awareness of it may be limited.⁷ In addition, some eligible families have the IRS compute their federal credit and may not receive a state EITC if the state does not compute the state credit amount for them. For these and other reasons, the cost of a refundable state EITC in its initial years will likely be lower than the full cost of the federal credit multiplied by the state percentage. To account for this, the cost estimate should be reduced by at least 10 percent.

The Results

The last three columns of Table 1 show the estimated fiscal year 2020 costs of providing a refundable EITC for tax year 2018 set at 5, 10, or 20 percent of the federal credit. Other percentages may be calculated based on those numbers; for instance, a 15 percent credit would cost one-and-a-half times as much as a 10 percent credit. The methodology outlined above may be used for other years using the projections of federal costs presented in Table 1.

None of these figures includes the costs of changing tax forms to include a space to claim an EITC or the costs of processing and administering EITC claims; these would likely raise the overall cost of the credit by less than 1 percent. The estimates presented here apply only to credits that are refundable and are set at a flat percentage of the federal EITC.

⁶ Refundable state credits range from 3 percent to 40 percent of the federal credit except for the District Columbia, where workers without qualifying children receive 100 percent of the federal credit. California's credit is worth up to 85 percent of the federal credit for workers earning up to \$7,800, depending on family size, and it is only available to workers earning up to about \$30,000, also depending on family size; in 2019, the maximum credit ranges from \$240 for workers without dependent children to about \$3,000 for workers with three or more children, plus a new \$1,000 Young Child Tax Credit for families with children under 6. (The value of the credit is set each year by the legislature.) South Carolina's non-refundable EITC will rise to 125 percent of the federal credit by 2023, but in dollar terms it is about half as generous as a refundable EITC worth 5 percent of the federal credit, because families with low incomes tend not to owe much in state income taxes.

⁷ Compared to the cost if every family claiming the federal credit also claimed the state credit, the actual cost of a newly enacted state EITC in its first year of availability was about 81 percent in Vermont, 83 percent in New York, 85 percent in Wisconsin, 88 percent in Oklahoma, 90 percent in Kansas and Minnesota, and 97 percent in Massachusetts. In the EITC's second year of availability, the cost (relative to the full-participation cost) rose to 85 percent in Vermont, 90 percent in New York, and 93 percent in Minnesota.

TABLE 1

Estimated Cost of Refundable State Earned Income Tax Credits, Fiscal Year (FY) 2021

State	Federal EITC Claims in Tax Year 2017 (\$ in thousands)	Percent of Total U.S. EITC Claims, Tax Year 2017	Estimated Federal EITC Claims in FY 2021 (\$ in millions)	Estimated Cost of State EITC in FY 2021* (\$ in millions)		
				Set at 5% of Federal Credit	Set at 10% of Federal Credit	Set at 20% of Federal Credit
States Without Refundable EITCs						
Alabama	1,377,983	2.11%	1,542	69	139	278
Alaska	102,377	0.16%	115	5	10	21
Arizona	1,505,440	2.30%	1,684	76	152	303
Arkansas	782,530	1.20%	876	39	79	158
Delaware**	176,936	0.27%	198	9	18	36
Florida	5,431,411	8.31%	6,077	273	547	1094
Georgia	2,973,266	4.55%	3,327	150	299	599
Hawaii**	215,515	0.33%	241	11	22	43
Idaho	303,211	0.46%	339	15	31	61
Kentucky	956,525	1.46%	1,070	48	96	193
Mississippi	1,072,988	1.64%	1,201	54	108	216
Missouri	1,215,956	1.86%	1,360	61	122	245
Nevada	636,511	0.97%	712	32	64	128
New Hampshire	145,955	0.22%	163	7	15	29
North Carolina	2,311,342	3.54%	2,586	116	233	465
North Dakota	94,608	0.14%	106	5	10	19
Ohio**	2,262,222	3.46%	2,531	114	228	456
Oklahoma**	859,194	1.32%	961	43	86	173
Pennsylvania	2,096,059	3.21%	2,345	106	211	422
South Carolina**	1,244,117	1.90%	1,392	63	125	251
South Dakota	136,638	0.21%	153	7	14	28
Tennessee	1,600,498	2.45%	1,791	81	161	322
Texas	7,328,229	11.22%	8,199	369	738	1476
Utah	436,956	0.67%	489	22	44	88
Virginia**	1,417,038	2.17%	1,585	71	143	285
West Virginia	350,692	0.54%	392	18	35	71
Wyoming	78,940	0.12%	88	4	8	16
Other Jurisdictions	43,658	0.07%	49	2	4	9
States With Refundable EITCs						
California	6,995,394	10.71%	7,827			

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Colorado	772,345	1.18%	864			
Connecticut	493,314	0.76%	552			
District of Columbia	120,809	0.18%	135			
Illinois	2,419,459	3.70%	2,707			
Indiana	1,280,913	1.96%	1,433			
Iowa	465,097	0.71%	520			
Kansas	487,609	0.75%	546			
Louisiana	1,447,387	2.22%	1,619			
Maine	208,390	0.32%	233			
Maryland	954,784	1.46%	1,068			
Massachusetts	835,558	1.28%	935			
Michigan	1,944,364	2.98%	2,175			
Minnesota	727,834	1.11%	814			
Montana	168,363	0.26%	188			
Nebraska	310,542	0.48%	347			
New Jersey	1,419,192	2.17%	1,588			
New Mexico	516,157	0.79%	578			
New York	3,994,797	6.11%	4,470			
Oregon	576,800	0.88%	645			
Puerto Rico***	n/a	n/a	n/a			
Rhode Island	188,670	0.29%	211			
Vermont	84,124	0.13%	94			
Washington	935,286	1.43%	1,046			
Wisconsin	830,147	1.27%	929			
Total	65,334,130	100%	73,096			

* Estimates assume that the cost of a state EITC will be 90% of the cost of the federal EITC in each state.

** For Delaware, Hawaii, Ohio, Oklahoma, South Carolina, and Virginia, cost shown is the total cost of a refundable credit; since those states already offer non-refundable credits, the added cost of making the credit refundable would be substantially less than the amount shown.

*** Puerto Rico adopted a local EITC in December 2018. Puerto Rican families are not allowed to claim the federal EITC, which means that the credit could not be set as a percentage of the federal EITC despite its similar design. Like state credits, it is substantially smaller than the federal EITC. Unlike most state credits, it phases in and out more quickly than the federal credit. For additional information, see Javier

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Balmaceda, "Puerto Rico on Verge of Implementing an EITC," Center on Budget and Policy Priorities, December 10, 2018, <https://www.cbpp.org/blog/puerto-rico-on-verge-of-implementing-an-eitc..>

Source: State claims data from Historic Table 2 State Data Tax Year 2017. FY 2021 cost calculated based on Joint Committee on Taxation estimates using Congressional Budget Office macroeconomic forecasts.