



KIDS COUNT in Delaware Issue Brief

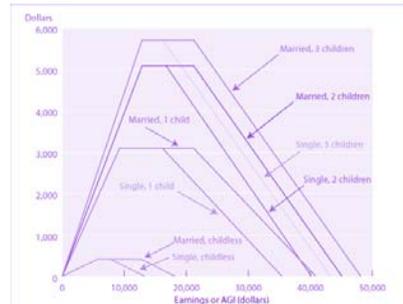


Delaware's Earned Income Tax Credit (EITC)

Spring 2011

The Earned Income Tax Credit (EITC) is the nation's most effective anti-poverty program for working families. This cash assistance program is targeted at low-income families and has been successful at encouraging people, particularly single mothers to take jobs. The EITC serves many public policy goals including: reduce child poverty, cut taxes for low-income families, increase incentive to work, stabilize income and spur consumption. Despite the success of the federal EITC in reducing poverty among working families, wages plus the EITC do not guarantee an escape from poverty for all families. State level EITCs sometimes help to fill that gap. In Delaware, the non-refundable EITC is set at 20% of the federal credit. A non-refundable EITC may offer substantial tax relief to families with state income tax liability, but it offers no benefits to working families that have income too low to owe any income taxes.

Earned Income Tax Credit By Filing Status and Number of Children, 2010



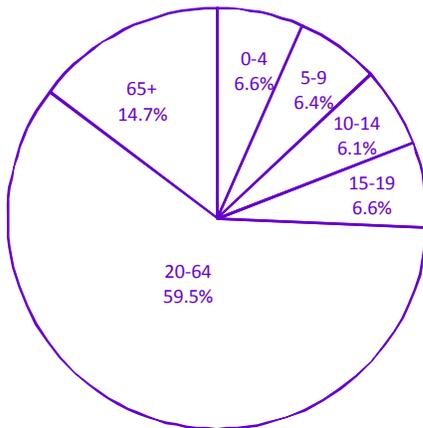
Source: Tax Policy Center– Urban Institute & Brookings Institution

The Earned Income Tax Credit (EITC) is an expression of a fundamental social contract: all Americans who can work should be able to support themselves and their families and not be poor.

~Metropolitan Policy Program at Brookings

Counting the Kids: Delaware Demographics

2010 Population Estimate and Age Distribution, Delaware



Delaware Total	895,173
Total Children 0-19	230,824
Children 0-4	58,675
Children 5-9	57,637
Children 10-14	54,994
Children 15-19	59,518

Demographically speaking, we are much less of a child centered society now than we were 100 years ago. In the United States, children accounted for 40 percent of the population in 1900, but only 26 percent in 2010. Similar trends are evident in Delaware.

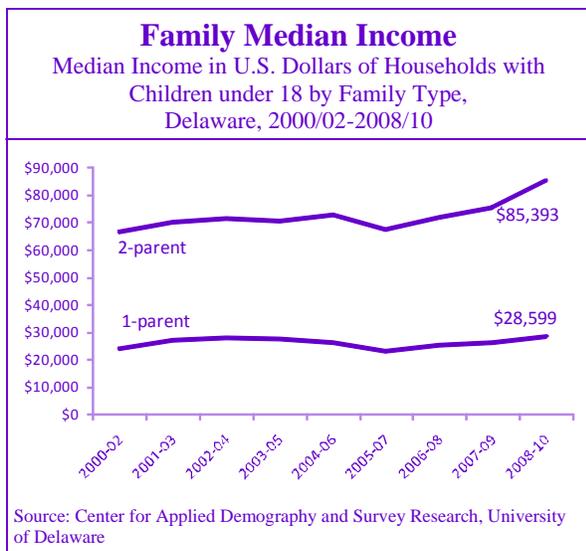
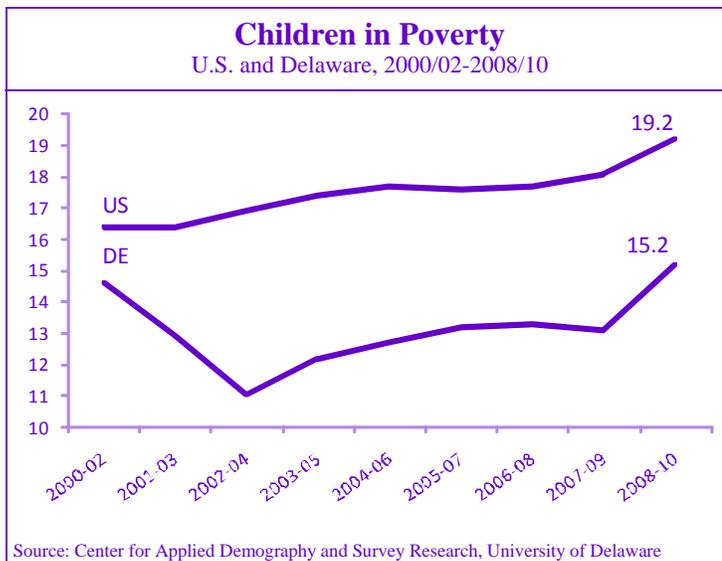
Source: Delaware Population Consortium, Population Projection Series, Version, 2010.0

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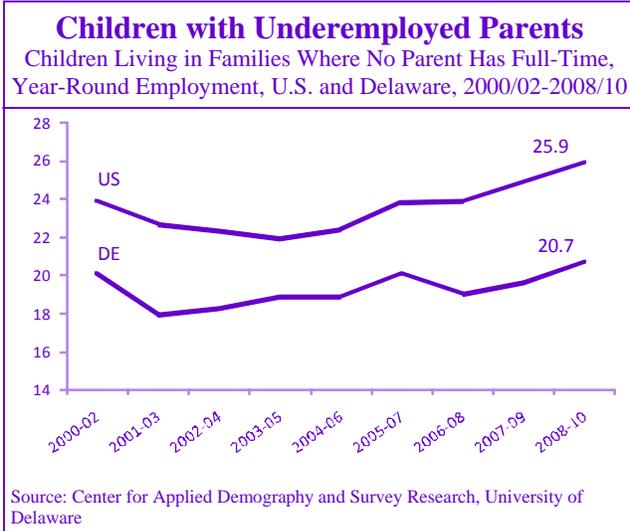
Delaware's Working Poor Families

Low wages mean that millions of parents in the U.S. work full time, year round and yet struggle to provide even a minimum of day-to-day necessities for their families. In other words, many low income families are poor despite work. A full time job at the minimum wage often is not sufficient to lift a family out of poverty. The number of families living below the poverty level has long been an important measure of economic stability. Economic hardship can have profound effects on children's development and their prospects for the future.



The official poverty threshold (\$21,954 for a family of four in 2009), falls well short of what it takes to provide a family with even the most basic necessities. Children living in two-parent households are much less likely to be in poverty than their peers living in one-parent households.

According to the Delaware Department of Labor, the state shed nearly 12,000 jobs in 2009. Because of the decrease in available jobs and greater competition for those jobs, a number of qualified workers were forced to take low pay jobs, part-time jobs or jobs beneath their skill level. This is commonly referred to as 'underemployment.' The losing streak was broken in January 2010 when there was a net gain of 500 jobs within the state.





Taxes in Delaware

The tax system has a pervasive impact on poverty, both directly through its role in the distribution of society's resources and indirectly through its effects on the incentives for economic decisions like working and saving. The two most important facets of the tax system for low-income families are payroll taxes and the Earned Income Tax Credit (EITC), the former of which levies a tax on earned income and the latter provides a tax credit for earned income.

Income tax systems serve low income families better than a state tax system that does not include an income tax at all because these are progressive.

Delaware's progressive features:

- ★ Income tax uses a graduated rate structure
- ★ Provides an exemption credit in place of personal exemption
- ★ No statewide sales tax

Delaware's regressive features:

- ★ Fails to offer refundable income tax credits to offset the impact of excise and property taxes

State & Local Taxes								
Delaware, 2007								
	Income Group	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Top 20%		
						Next 15%	Next 4%	Top 1%
	Income Range	< 19,000	\$19,000-\$33,000	\$33,000-\$56,000	\$56,000-\$90,000	\$90,000-\$171,000	\$171,000-\$422,000	\$422,000 or more
Sales/Excise Taxes		3.3%	2.3%	1.5%	1.3%	1.0%	0.5%	0.2%
Property Taxes		2.1%	1.9%	1.6%	1.6%	1.6%	1.3%	0.7%
Income Taxes		0.6%	1.9%	2.7%	3.2%	3.8%	4.1%	4.7%
Total Taxes		6.0%	6.1%	5.8%	6.1%	6.4%	5.8%	5.6%
Federal Deduction Offset		-0.0%	-0.1%	-0.3%	-0.6%	-1.2%	-1.1%	-1.1%
Total After Offset		6.0%	6.0%	5.4%	5.5%	5.2%	4.8%	4.5%

Source: Institute on Taxation and Economic Policy, "Who Pays? A Distributional Analysis of the Tax System in All 50 States" 3rd Edition Nov 2009

State Income Tax Thresholds	
Two Parent Family of Four, Delaware, 1999-2009	
1999	\$8,600
2000	\$20,300
2007	\$29,300
2008	\$30,100
2009	\$31,700

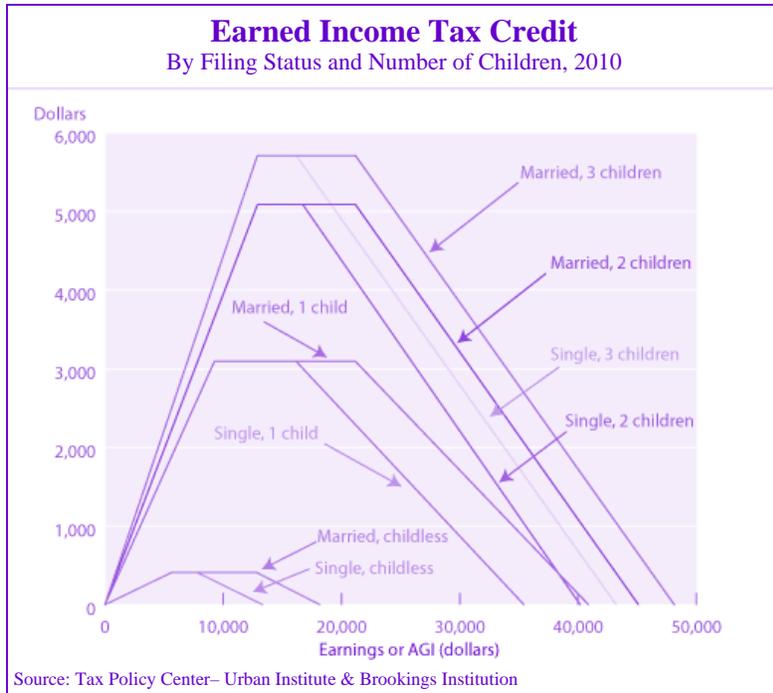
Source: Center on Budget and Policy Priorities

According to the Delaware Department of Finance, Division of Revenue, Delaware has a graduated income tax rate ranging from 2.2% to 5.55% for income under \$60,000 and 6.95% for income of \$60,000 or over.

Increases to the state income tax threshold over time mean that workers may earn more without owing state income tax. The impact on EITC... a non-refundable EITC (like our state level credit) can only be used to offset tax liability. It offers no benefits to working families that have income too low to owe income taxes.



Tax Credit for Working Poor Families - The Federal EITC



The federal EITC was introduced in 1975 and was designed to offset federal income taxes and social security payroll taxes, supplement earnings and reward work. The credit varies with income levels and is adjusted annually for inflation. The federal credit is refundable—policy makers recognized that the income tax is not the only federal tax paid by low- and middle-income workers. These taxpayers usually pay much more in payroll taxes than in income taxes. By making the EITC refundable, Congress ensured that it could be used to help offset all federal taxes paid, not just the income tax. Its design also reflects the reality that larger families face higher living expenses than smaller families.

In 2009, the EITC lifted an estimated 6.5 million people (including 3.3 million children) out of poverty.

Income Limits & Maximum Credit Amounts
EITC, 2010

# of Qualifying Children	Single, Income Must be Less Than	Married Filing Jointly, Income Must be Less Than	Range of EITC
0	\$13,460	\$18,470	\$2 - \$457
1	\$35,535	\$40,545	\$9 - \$3,050
2	\$40,363	\$45,373	\$10 - \$5,036
3+	\$43,352	\$48,362	\$1 - \$5,666

Source: Internal Revenue Service

The EITC garners non-partisan support because it rewards work. It enjoys broad backing, with support from business groups, labor, faith-based organizations and social service advocates.

EITC has been shown to increase workforce participation among eligible families.

The EITC is used by many recipients for asset-building purposes. Many EITC refunds are utilized to make the kinds of investments (paying off debt, obtaining education, securing decent housing) that enhance economic security and promote opportunity.

Federal EITC Benefits
Delawareans, 2009

Delawareans who qualified for federal EITC	69,368
Average tax break	\$2,100
Total federal EITC claimed by DE residents	\$145,690,147

Source: Internal Revenue Service



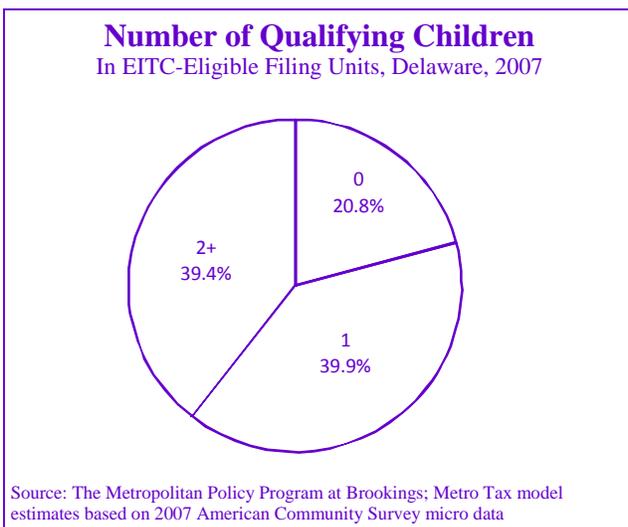
Tax Credit at the State Level- Delaware's EITC

Despite the success of the federal EITC in reducing poverty among working families, wages plus the EITC do not guarantee an escape from poverty for all families. In other words, the federal EITC alone does not lift all working families out of poverty. State EITCs are simple to implement, administer and claim. These programs typically “piggyback” on the federal EITC meaning that they mostly have the same eligibility requirements and are set at a fixed percentage. As a result, states can take advantage of the existing federal statutory structure and compliance apparatus so filers need only multiply their federal EITC by a specified rate to determine their state credit. Nonrefundable credits can only be used to offset income tax liability, even though sales and property taxes are usually more burdensome for low-income working taxpayers.

Delaware's 143rd General Assembly passed Senate Bill 230 which establishes a non-refundable state level earned income tax credit equal to 20% of the corresponding federal tax credit.

State Level EITC Delaware, 2008	
Delawareans who qualified for state EITC	66,152
Delaware EITC	20% of federal (non-refundable)
Total state EITC claimed by DE residents	\$6 million
Source: Center on Budget and Policy Priorities	

Characteristics of EITC-Eligible Tax Filers Delaware, 2007			
Top Five Occupations:		Top Five Industries:	
Office Administration	18.2%	Retail Trade	14.9%
Maintenance	9.6%	Accom/Food Service	10.9%
Sales	9.1%	Construction	10.3%
Food Preparation	8.9%	Healthcare	9.3%
Construction/Mining	8.6%	Administrative Services	8.3%
Source: The Metropolitan Policy Program at Brookings; Metro Tax model estimates based on 2007 American Community Survey micro data			



In 2010 tax year, 23 states had a state level EITC. Most are refundable. Only Delaware, Maine and Virginia offer non-refundable credits. Such credits are available only to the extent that they offset a family's state income tax. A non-refundable EITC still can provide substantial tax relief to families with state income tax liability, but it offers no benefits to working families that have income too low to owe any income taxes.

In 2009 in Delaware, the tax threshold for a family of 4 was \$31,700. Working families that earned less than this threshold did not qualify for a refund at the state level via the Delaware version of Earned Income Tax Credit.



Outreach and the Economy

Credits via the EITC are only granted to those taxpayers who apply for them, which means that efforts to raise public awareness of the credit are essential to ensuring that the credit lives up to its potential. The IRS estimates that 20 to 25 percent of qualifying workers miss out on thousands of dollars every year because they fail to claim their EITC. This includes workers who are:

- ★ Living in rural areas,
- ★ Self-employed,
- ★ Receiving certain disability pensions or have children with disabilities,
- ★ Without a qualifying child,
- ★ Not proficient in English,
- ★ Grandparents raising their grandchildren or
- ★ Recently divorced, unemployed or who experienced other changes to their marital, financial or parental status

Critics complain that the EITC is too complex, forcing potential recipients to seek help filing their federal tax return: two thirds of low income parents get such assistance, typically from paid tax preparers.

The three major factors that account for a drain on EITC funds are tax preparation fees, refund anticipation loans and other products and fees.



Delaware Earned Income Tax Credit (EITC) Campaign

Founded and Operated by Nehemiah Gateway CDC

Tax Awareness, Free Tax Preparation, and Financial Services

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The Delaware EITC Campaign, founded and operated by Nehemiah Gateway CDC, is part of a comprehensive strategy to elevate the standard of living and cash flow of Delaware residents. Coordinating efforts among a broad array of organizations from the public, private, faith-based and non-profit sectors, the Campaign:

- ★ Promotes awareness of the EITC to workers with household incomes under \$38,000
- ★ Offers free income tax preparation with the IRS' Volunteer Income Tax Assistance (VITA) Program. A list of these sites can be found on the Campaign's website: www.eitcdelaware.net
- ★ Links customers to information and services that increase economic self-sufficiency

Impact of the 2009 Recession

According to the Center for Budget and Policy Priorities, the number of working poor has increased in each of the last three recessions. The recent recession has sharply reduced state revenues in Delaware and across the nation.

Per some indicators of economic well-being, the U.S. economy began to improve in late 2009. However, it is expected to be quite some time before unemployment levels, family incomes and stable job levels return to pre-recession era levels. Many experts suggest that the on-going effects of the recession will not only persist, but also be severe.

The American Recovery and Reinvestment Act (ARRA) provided a temporary increase in the Earned Income Tax Credit (EITC) for taxpayers with three or more qualifying children and increased the beginning point of the phase-out range for the credit for all married couples filing a joint return for 2009 and 2010. The Tax Relief and Job Creation Act of 2010 extended these changes to 2011 and 2012.



Moving Forward

Credits are Good for Local Economies

State tax credits for low-income families put money into the hands of people most likely to spend it, and most likely to spend it in their local economy. During an economic downturn, generating more demand for goods and services is what creates and preserves jobs. Businesses are more likely to hire and retain employees and to maintain or increase orders from their suppliers when they see increased consumption of their products or services. Low income families spend virtually all of their income to make ends meet and they tend to spend it locally. So tax credits quickly wind up benefitting local employers. A refundable EITC also promotes asset building! Recipients also may elect to use refunds to pay off debt, to obtain education or to secure decent housing. Each of these investments are those that enhance economic security and promote opportunity.

The Earned Income Tax Credit (EITC) is an expression of a fundamental social contract: all Americans who can work should be able to support themselves and their families and not be poor.

~Metropolitan Policy Program at Brookings

State refundable tax credits targeted at low-income working families encourage work, stabilize income and spur consumption. In moving forward to reduce poverty and encourage work, legislators must preserve past efforts and build upon them as the fiscal situation improves.



Balancing Budgets

Tax measures that reduce the incomes of high-wealth individuals and corporate shareholders are more likely to be paid from savings and retained earnings, so they will have relatively little effect on how much those individuals spend. Reductions in the after-tax incomes of low income families on the other hand have a greater impact on consumption and hence the overall economy, thus are far more beneficial to state economies than tax cuts for wealthy individuals which generally do not increase consumption.

According to the Center on Budget and Policy Priorities, existing refundable EITCs in states with income taxes produce a revenue loss of less than 1 percent of state tax revenues each year. Though low-income households tend to comprise a substantial share of all taxpayers, the share of tax revenue they account for is much lower. A few hundred dollars for each family makes a big difference to the family's ability to make ends meet without adding up to a major dent in a state's treasury.

Recommendations

- ★ Make the state level Earned Income Tax Credit refundable in Delaware ★
- ★ Increase Delaware's percentage of the federal credit from 20 to 40 ★
- ★ Make non-custodial dads eligible for EITC conditional to their child support payments ★
- ★ Establish a bonus if EITC funds are deposited into a savings or investment account ★

