

POLICY BRIEF

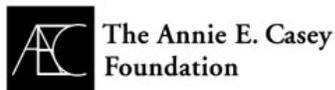
Refundable Tax Credits

A Permanent Solution for Working Families



September 2010





TheJoyceFoundation



The National Community Tax Coalition would like to acknowledge the Rockefeller Foundation for their generous support of our tax credit policy work. Additional support is provided by the Annie E. Casey Foundation, the Joyce Foundation, and the W.K. Kellogg Foundation.

NCTC Policy Staff

Jackie Lynn Coleman, Senior Director
Gregary Brown, Director of Policy and Research
Lucy Mullany, Manager, Government Relations
Holden Weisman, Policy Analyst

For comments or questions, please contact Lucy Mullany at (312) 252-0280, ext. 270 or lmullany@economicprogress.org.

Table of Contents

I. Executive Summary	5
II. Beyond Recovery	7
A. Growing GDP is relatively easy, getting people back to work is not	7
B. America’s middle-class remains vulnerable	8
C. Higher education is the key to job security	8
III. How Did ARRA Change the Tax Code?	9
A. Child Tax Credit	9
B. Earned Income Tax Credit	12
1. A New Tier for Families With Three or More Children	12
2. Reduction of the Marriage Penalty for All EITC Recipients	13
C. American Opportunity Tax Credit	13
D. Making Work Pay Tax Credit	14
IV. What the Recovery Act Did Not Accomplish	16
A. Expand the EITC for Childless Workers	16
B. Reform the Saver’s Credit	17
V. Potential Offsets	18
VI. Conclusion	20
VII. Appendices	21
A. Appendix A: Taxpayer Scenarios	21
B. Summary of American Recovery and Reinvestment Act Tax Provisions for Working Families	25
C. Distribution of Tax Benefits	26
VIII. End Notes	27

About the National Community Tax Coalition

A project of the Center for Economic Progress, the National Community Tax Coalition (NCTC) works to create a more accessible and equitable tax system for American workers. NCTC is a national network dedicated to strengthening economies, building communities and improving lives through tax assistance and asset building activities that produce financial security, protect families, and promote economic justice.

Our network of organizations provides critical, on-the-ground financial services for working families. NCTC represents the 12,000 community Volunteer Income Tax Assistance (VITA) sites nationwide that collectively prepare an estimated 3 million tax returns for low- and moderate-income workers. Community tax preparers offer a high-quality choice – one that’s free, accessible, and equipped to help families claim their full refund and all the credits to which they are entitled.

We actively seek to broaden the reach and impact of community tax preparers and are a leading voice in Washington, DC for low-wage workers and against unfair financial practices. We believe that together, we can strengthen economies, build communities and improve life for all American families.

National Community Tax Coalition
29 E. Madison Street, Suite 900
Chicago, IL 60602
(312) 252-0280
www.tax-coalition.org

Executive Summary

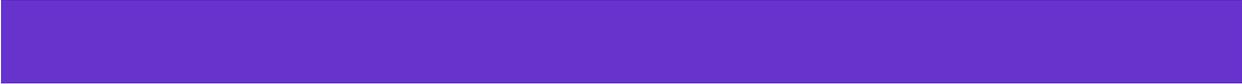
In 2009 Congress passed the American Recovery and Reinvestment Act (ARRA or the Recovery Act), a package of tax cuts and spending initiatives designed to boost the nation's ailing economy. Experts estimate that ARRA added 2.7 million jobs and increased Gross Domestic Product (GDP) by 3.4 percent.¹ ARRA's success is in part attributable to the expansion of existing tax credits and the creation of new credits aimed at working Americans. With these reforms, Congress took a major step toward creating a more fair tax code that values families, a strong work ethic and higher education.

Congress enacted ARRA as a temporary measure in response to the recession, and thus the tax cuts for working families are scheduled to expire at the end of 2010. For advocates of a fairer tax system, the ARRA tax cuts were not a one-off fix, but part of a long-term solution for working families. The Recovery Act achieved many of the reforms we supported long before the economic downturn, including the expansion of the Earned Income Tax Credit (EITC) and Child Tax Credit (CTC), as well as the creation of new refundable tax credits. These vital credits, and the progressive nature of our tax system overall, are now at risk.

The National Community Tax Coalition urges Congressional leaders, as they debate extending the 2001 and 2003 tax legislation, to make the ARRA tax cuts for working families permanent.² Failure to act will not only jeopardize the fragile economic recovery, but also raise taxes on moderate- and middle-income families and undo what was a major step forward.

Four ARRA Reforms that Made a Difference

1. **Child Tax Credit:** Counted earnings below \$13,000 toward the refundable part of the tax credit.
2. **Earned Income Tax Credit:** Added a new tier for families with three or more children and reduced the marriage penalty.
3. **American Opportunity Tax Credit:** Replaced the existing HOPE education credit with a \$2,500 credit that is refundable up to \$1,000 and covers required course materials (e.g., books and supplies) in addition to tuition, making college more affordable.
4. **Making Work Pay Credit:** Created a new refundable tax credit of \$400 (\$800 for married couples filing jointly) that benefits 95 percent of working Americans, but could have been more efficiently targeted at low- and moderate-income workers.



This policy brief is broken up into four sections. Section 1, *Beyond Recovery*, explains why refundable tax credits are important to the economy's long-term health. Section 2, *How Did ARRA Change the Tax Code*, summarizes each of the four credits and explains what changes were made under ARRA. While ARRA changed the tax code for the better, Section 3, *What the Recovery Act Did Not Accomplish*, discusses several policies that did not make it into the legislation, but should be a part of future legislation. Section 4, *Potential Offsets*, highlights suggested offsets to cover cost of making the ARRA provisions permanent. Appendix A provides several scenarios, showing how failure to make the ARRA provisions permanent will increase taxes on working individuals and families, while Appendix B summarizes the four major tax credits in table format. Lastly, Appendix C is a visual representation of the distribution by income quintile of the EITC, CTC and Making Work Pay Credit and the percentage of households receiving each tax credit.

Beyond Recovery

Eliminating the ARRA tax credits will not only damage the short-term recovery, but also hurt the long-term prospects for working families. Whereas gross domestic product (GDP) began to grow in 2009, the labor market is expected to remain soft well into 2012.³ During this time, a significant percentage of America's middle class will continue to face long bouts of unemployment and lower wages. Chronic unemployment, decreased benefits and continued financial pressures have taken a toll on the psyche of American workers. Refundable tax credits are instrumental to getting Americans back to work.

And, for those families who silently suffered through depression-like conditions well before the recession struck, refundable tax credits will continue to play a vital role. Refundable tax credits like the EITC and CTC help address financial gaps for many Americans working at poverty-level wages, while offering a proven work incentive and a gateway to higher-wage occupations. ARRA's extension of these tax credits, coupled with the introduction of the American Opportunity Tax Credit (which opened the door to higher education for many low- and middle-income Americans) reaffirmed these positive attributes.

Working families will not measure today's economic recovery in days or months, but in years. Expanding refundable tax credits during the recession was necessary, but it is no less important to make these credits a permanent part of the tax code. American families were more vulnerable than anyone imagined and will continue to remain so unless Congress takes action to put the U.S. economy and hard-working families on firmer footing. Refundable tax credits are one way to address the following three lessons we learned from the Great Recession.

1. Growing the GDP is relatively easy, but getting people back to work is not. The U.S. is at serious risk of creating a permanent underclass consisting of the long-term unemployed and discouraged workers.

As of July 2010, 6.6 million workers have been unemployed for more than half of year, while the average unemployed worker has spent 34 weeks searching for a job.⁴ An additional 1.2 million "discouraged" workers left the labor force altogether.⁵ When the job market does eventually turn around, it will be important to offer marginalized workers an incentive to re-join the labor force. While refundable tax credits like the EITC have traditionally drawn low-skill workers into the job market, these credits may play a renewed role as long-term jobless

workers who once had a strong attachment to the labor force and decent jobs must now overcome the trauma of being without a job for months on end, while facing the prospect of lower wages.

2. America's middle-class remains vulnerable. During the recession, the position of solidly middle-class families proved to be more precarious than anyone could have imagined.

Due to unemployment, underemployment and lower wages, median family income fell from \$52,163 to \$50,303 between 2007 and 2008.⁶ But lost income is only a small part of the story. For many families, a single bout of extended joblessness wiped out long-term savings and cost millions of individuals and families their homes.

As of August 2010, household wealth was down \$14.8 trillion compared to June 2007, while household debt as a percentage of income remained over 120 percent.⁷ Between lower wages and the sudden loss of wealth, it's not surprising that credit card defaults as a percentage of credit card debt during the first quarter of 2010 were 134 percent higher than when the recession began at the end of 2007 and that one in seven mortgages is either delinquent or in foreclosure.⁸ Tax policy alone cannot restore the middle-class, but refundable tax credits can help families to get back on their feet, while beginning to pay down debt and to rebuild savings.

3. Higher education is the key to job security. Refundable education credits make college more affordable for working families and nontraditional students.

A college education was perhaps the greatest defense against unemployment throughout the recession. Compared to workers with a bachelor's degree, people with only a high school diploma were two times as likely to be unemployed over the past two years. Similarly, workers with an associate's degree were unemployed at a substantially lower rate than their less-educated counterparts.

Given the value of higher education, it is disturbing that the U.S., once the world leader, is now 12th among developed nations as measured by the percentage of young adults who have completed a college education. Within the U.S., fewer than one out of five young adults has an associate's degree (or higher) in much of the South and Southwest, while minority students throughout the U.S. who enroll in two- and four-year degree programs are far less likely to complete their programs than the population at large.⁹

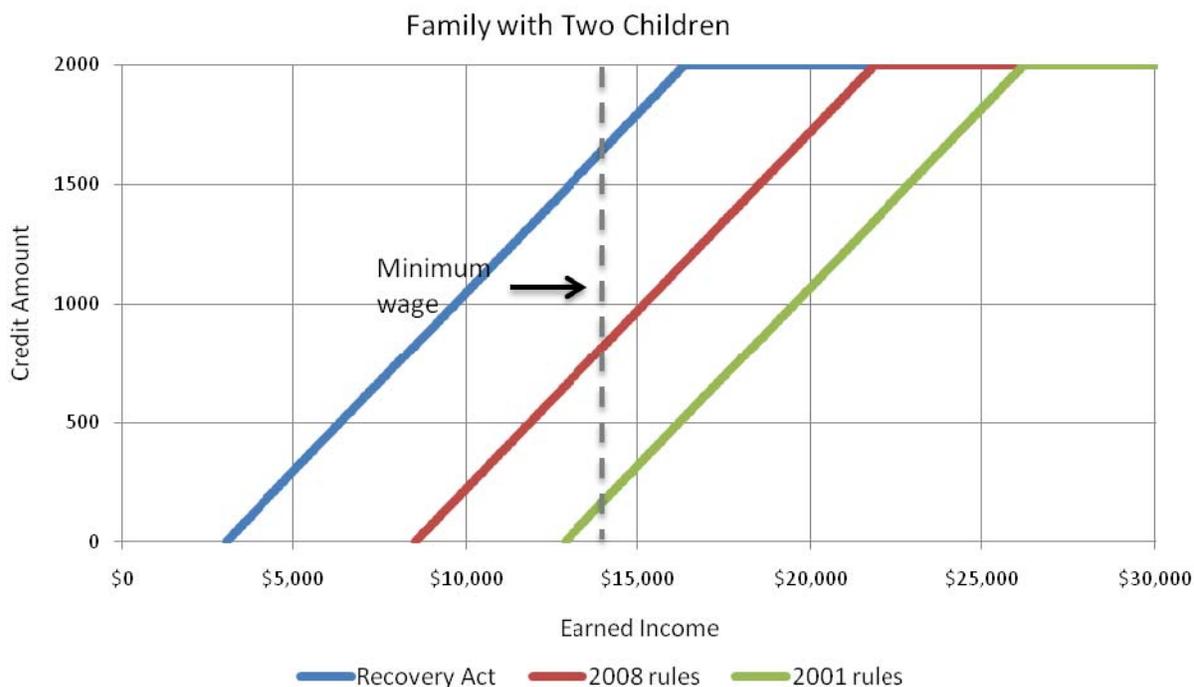
How Did ARRA Change the Tax Code?

As the examples below demonstrate, it is important to remember that the tax credits outlined in ARRA do not work in isolation, and the Recovery Act was developed in such a way as to create a holistic package of multiple tax credits for American families. For example, if the ARRA provisions are not extended, parents with young children and a child in college could lose part of the CTC, the EITC, education credits and all of the Making Work Pay Credit. The cumulative impact of losing these tax credits can be in the thousands of dollars, which is not a small amount of money for moderate- and middle-income families.

CHILD TAX CREDIT

Since the creation of the CTC in 1997, Congress endorsed two positive changes over the past decade to enhance the credit and make it more accessible for working families. First, Congress has increased the value of the CTC from its original level of \$500 per child to \$1,000 per child. Second, Congress took steps to make the CTC available to moderate-income families. However, until the Recovery Act, many parents working full-time still received little or no benefit from the credit because earnings up to a specified point were not taken into consideration when calculating the refundable portion of the tax credit. **Congress lowered the threshold to \$8,500 in 2008, and the ARRA reduced this amount further to \$3,000 for 2009 and 2010.** The expanded CTC provides an important incentive for parents to work while giving them the financial boost they need to support themselves and their children.

Figure 1. 2001 and 2008 Rules Substantially Reduce Child Tax Credit for Working Families



Source: National Community Tax Coalition modification of Figure 1 in Sherman, Arloc, Avi Feller and Chuck Marr, *Failure to Extend Improvements in the Child Tax Credit Would Harm Millions of Low-Income Working Families*, Center on Budget and Policy Priorities (Feb. 2010).

If Congress were to continue the 2001 and 2003 tax cuts, but fail to extend either the 2008 or Recovery Act provisions, earnings up to \$12,850 will not count toward the credit in 2011.¹⁰ An analysis by the Center on Budget and Policy Priorities found that failure to extend the Recovery Act legislation will have the largest affect on aspiring middle-class families:

- Working parents earning between \$12,850 and \$16,333 will suffer the largest monetary losses;
- Families earning over \$10,000 will bear 80 percent of total losses;
- Parents of 7.6 million children will lose all of their CTC; and
- Parents of an additional 10.5 million children will see their credit reduced.¹¹

Whereas a married couple with two children must earn \$16,335 to claim the maximum credit (\$2,000) under the ARRA tax provisions, their required earnings to receive the full credit would increase to \$21,830 under the 2008 rules and \$26,180 with the 2001 threshold in place. A family with one parent working full-time at the minimum wage would receive almost no benefit under the 2001 rules (**figure 2**).

Figure 2. Child Tax Credit for Family Earning Minimum Wage, 2011

Source: Center on Budget and Policy Priorities.

Failure to extend the Recovery Act rules will have a significant impact on millions of working parents. A family with one minimum wage earner stands to lose as much as \$1,500 (**figure 2**). It makes little sense to take \$1,500 away from families who were hurt most by the recession, while allowing other parents to keep the full credit. It makes even less sense to take away the credit when many families and the communities where they live will still be recovering from the recession.

Scenario 1, Mother loses entire Child Tax Credit:

A single mother of one young child, earning \$12,800 per year will lose the entire \$1,000 CTC and the \$400 Making Work Pay Credit. After paying \$980 of Social Security and Medicare taxes, her income will be just above the poverty level.

Total income lost = \$1,400

Scenario 2, Mother loses part of the Child Tax Credit:

A single mother with two young children earning \$20,000 per year will see her CTC fall from the maximum value (\$2,000) to \$1,115. She will also lose the Making Work Pay Tax Credit, while paying \$1,530 in Social Security taxes.

Total income lost = \$1,285

EARNED INCOME TAX CREDIT

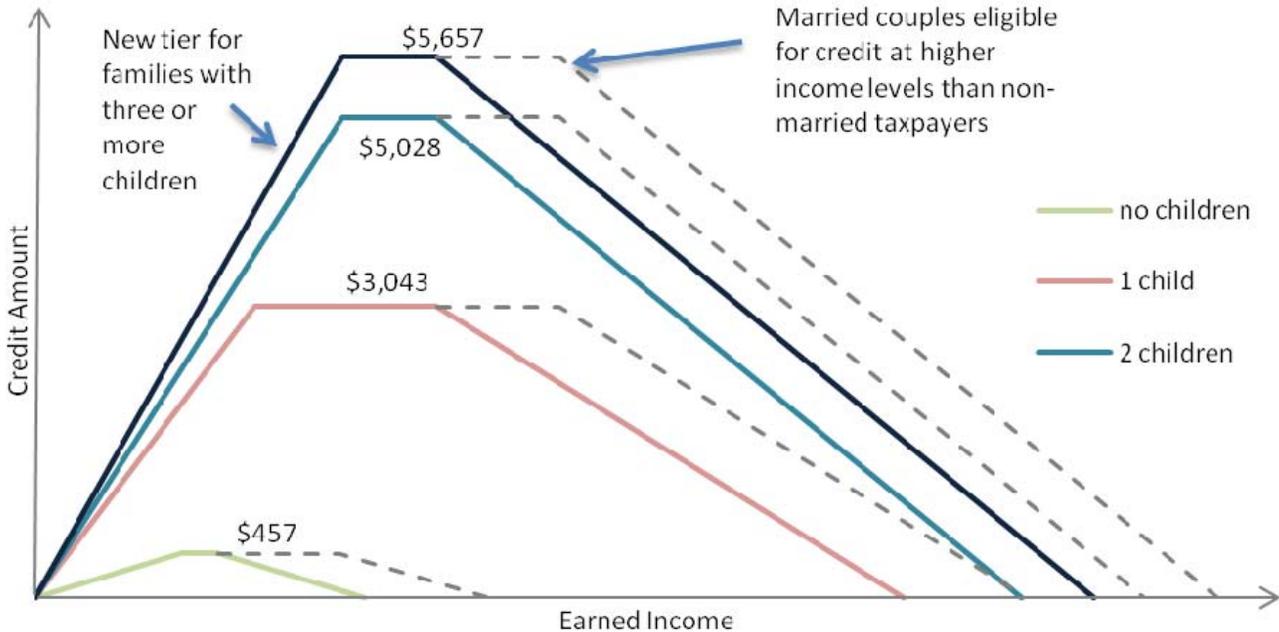
The Earned Income Tax Credit (EITC) amount is based on earnings as well as the number of children in a household. As earnings increase, the credit amount goes up, plateaus and eventually returns to zero (**figure 3**). Prior to ARRA, the maximum credit amounts in 2009 were: \$457 (no children), \$3,043 (one child) and \$5,028 (two children). **ARRA made two significant advances in 2009 and 2010.**

1. The Recovery Act added a new tier for families with three or more children.¹²

Research shows that families with three or more children are twice as likely to be in poverty than smaller families with fewer children.¹³ According to the Center on Budget and Policy Priorities, 3 million families and 10 million children will benefit from the new tier.¹⁴ In addition to increasing the maximum credit, the new tier also allows higher-income families with three or more children to access the EITC.

- The new tier for large families increased the maximum credit from \$5,028 to \$5,657.
- Families earning up to \$43,250 will be eligible for the credit (\$48,250 for married couples).

Figure 3. Earned Income Tax Credit, 2009



Source: National Community Tax Coalition analysis of IRS Earned Income Tax thresholds.

2. The Recovery Act reduced the marriage penalty for all EITC recipients.

Marriage penalties discourage single EITC recipients from getting married. For example, a low-income working mother may qualify for the EITC, but if she gets married to someone with similar earnings, there is a good chance that the combined family will lose their entire EITC. From a financial perspective, it may make more sense for the couple to remain unmarried. ARRA took steps to narrow the gap between married filing jointly and remaining unmarried.

- ARRA essentially shifted the dotted line in figure 3 to the right by \$1,880, thereby extending the income eligibility limit for married couples to \$5,000 over head of house hold and single filers.
- In addition, as the credit phases out, married couples will be able to claim a higher credit at each income level (the maximum and phase-in amounts are still the same for married couples and head of household and single filers).
- An estimated 5 million working families and 8 million children benefit from a reduced marriage penalty.¹⁵

If the Recovery Act provisions do not become permanent:

Scenario 3, Married couple with three young children faces an across-the-board tax increase:

A family of five earning \$30,000 loses the \$1,023 from the EITC due to the elimination of the new tier for families with three or more children and reduced protection from the marriage penalty. The family also loses the entire Making Work Pay Credit and is unable to claim the entire CTC. These parents pay \$2,295 of Social Security and Medicare taxes.

AMERICAN OPPORTUNITY TAX CREDIT

Prior to the creation of this new credit, education tax incentives, such as the tuition deduction, Hope Credit and Lifetime Learning Credit, went largely to upper-middle-class families. The Tax Policy Center estimates that in 2005, 42 percent of education tax benefits went to families earning over \$50,000.¹⁶ Meanwhile, nontraditional students and the children of working-class families were unable to take advantage of these incentives. Conventional wisdom maintains

that low- and moderate-income students do not need tax credits because they receive Pell grants and other forms of need-based financial aid, but this is not the case.

- Seven out of ten moderate-income students in four-year degree programs have unmet financial need.¹⁷
- The average unmet need is over \$4,000 annually for community college students and \$6,430 at a public four-year college or university.¹⁸

The American Opportunity Tax Credit replaced the \$1,800 Hope Credit for most taxpayers in 2009 and 2010, benefiting nearly 4 million students who would otherwise receive no education tax benefits.¹⁹

- The new education credit is worth up to \$2,500 (100 percent of qualifying expenses up to \$2,000 plus 25 percent of qualifying expenses between \$2,000 and \$4,000)
- Unlike existing incentives, the credit is partially refundable (up to \$1,000), which is why this new incentive is available to nontraditional students and lower-income families.
- Qualified expenses now include course materials (e.g. books and supplies), an added bonus for students attending community college where books account for a large part of total expenses.

If the Recovery Act provisions do not become permanent:

Scenario 4, Parents earning \$35,000 with a college student and two teenagers lose nearly \$3,000:

Without the American Opportunity Tax Credit, this family's education tax credit could fall from \$1,490 to only \$490, leaving them with \$1,000 less to cover tuition and books. They also are hurt by the elimination of the new EITC tier for large families and the marriage penalty reduction.

Total income lost = \$2,823

MAKING WORK PAY TAX CREDIT

The Making Work Pay Credit, President Obama's signature tax cut, reduces taxes for 95 percent of working Americans, but is unlikely to be made permanent. Even the President's own budget would let the credit expire after 2011. A \$60 billion per year price tag and the

reality that over half the credit's benefits accrue to middle- and upper-income families who need no work incentive made the credit unpopular with policymakers. However, the fact that this credit is likely to be eliminated is even more reason to make the other Recovery Act provisions permanent and to consider a more cost effective work incentive, such as an increase in the EITC for childless workers.

Table 1. Distribution of Making Work Pay Credit

Income Group	Percent with Tax Cut	Share of Total Tax Benefit	Average Tax Cut
Bottom	61.6	16.0	-230
Moderate	79.1	21.5	-367
Middle	86.7	23.6	-442
Upper-Middle	85.6	23.4	-523
Top	56.7	15.2	-384
Total	73.7	100.0	-374

Note: Bottom income group goes from \$0 to \$18,981; Moderate from \$18,982 to \$37,595; Middle from \$37,596 to \$66,354; Upper-Middle from \$66,355 to \$111,645; and Top is over \$111,645.

If the credit is eliminated, working families will lose up to \$800 (\$400 for unmarried taxpayers) in 2011. Because the fully refundable credit “phases in” quickly, reaching its peak value at earnings of \$12,900 (\$6,450 for unmarried taxpayers), the vast majority of low- and moderate-income workers receive the full credit amount. And unlike other tax benefits, even workers without children are eligible for the full value.

- If none of the Recovery Act provisions, including Making Work Pay, are extended, working families will see a substantial reduction in take home pay. A permanent expansion of the EITC and CTC will lessen the cumulative blow to families with children.
- Doubling the EITC for childless workers, which was not a part of the Recovery Act, would offer low-income workers the same work incentive as the Making Work Pay Credit for a fraction of the cost.

Scenario 5, Minimum wage worker with no children owes federal income tax and Social Security taxes:

Everyone talks about how low-income workers pay no taxes, but with the Recovery Act provisions in place, a full-time minimum wage worker with no children earning \$15,000 will still owe \$1,298 in federal taxes (Social Security, Medicare and income taxes). Without the Making Work Pay Credit, this worker's tax bill will go up an additional \$400.

What the Recovery Act Did Not Accomplish

As much as ARRA accomplished for workers, families and students, there are two additional policies that will be essential to long-term recovery. Prior to the recession, momentum built for an expansion of the EITC for childless workers as a way to bring less-educated young workers, and men in particular, into the labor force. However, this policy fell to the wayside in favor of the Making Work Pay Credit, which benefited moderate and middle-income workers as well. Now that the Making Work Pay Credit is likely to be eliminated, it is time for Congress to reconsider an expansion of the EITC.

Reform of tax credits focused on incentivizing savings is another popular idea that has yet to come to fruition. Over the past two years, American families began saving again for the first time in years. Savings enables families to pay for college, buy their first home and be prepared for an uncertain future. Reforming the primary savings incentive available to working families would build on one of the few positive trends to emerge from the recession.

Expand the EITC for Childless Workers

Economic research has shown that the EITC is a powerful work incentive as well as a gateway to higher earnings for single mothers.²⁰ Policymakers and economists believe that the credit could have the same impact on low-wage workers without children, if the credit was two to three times greater than the current amount (\$457). The existing EITC for this population is not only small, but is unavailable to full-time workers earning the minimum wage.

As of June 2010 there are 1.7 million unemployed workers with less than a high school education. Compared to college-educated workers, they are three times as likely to be unemployed. Likewise, one out of four African American men is unemployed. Less educated and minority workers faced a difficult labor market before the recession and are at risk of becoming permanently detached from the labor force. **An expanded EITC for people without children may be the most effective way to draw discouraged workers back into the labor force and to encourage them to search for jobs.**

Possible policy options include:

- Double (\$900) or triple (\$1,300) the maximum credit
- Increase the range in which the credit phases out to \$20,000
- Lower the eligibility age from 25 to 18 or 21

The Making Work Pay Credit costs over \$60 billion a year. For a fraction of that cost (approximately \$3 billion per year), Congress could double the EITC for childless workers.

Reform the Saver's Credit

Of the \$127 billion the federal government spends on retirement savings incentives, only \$900 million goes to the Saver's Credit.²² The Saver's Credit is the primary savings incentive offered to low- and moderate-income households, yet many potential savers are not even eligible for the non-refundable credit. And, because the credit is so confusing, few taxpayers are likely to understand how the incentive works. President Obama, members of Congress and think tanks have introduced numerous reform proposals. In general, these proposals would accomplish the following:

- offer a dollar-for-dollar match on savings up to \$500;
- expand eligible savings vehicles to include education savings accounts as well as U.S. savings bonds.

Potential Offsets

The estimated ten-year cost of extending the EITC, CTC and American Opportunity Education Credit is just under \$190 billion (**table 2**). This amount excludes the cost of the Making Work Pay Credit. Doubling the EITC for childless workers would add about \$30 billion over ten years.²⁴

Table 2. Ten-Year Cost of Extending Recovery Act Benefits, Fiscal Years 2011 to 2020

	Dollars (billion)	
	FY 2012	FY 2011 - FY 2020
Child Tax Credit (maintain \$3,000 earnings threshold)		
maintain \$3,000 earnings requirement	\$9.60	\$83.10
Earned Income Tax Credit		
tier for families with 3 or more children	\$1.70	\$15.20
marriage penalty reduction	\$1.70	\$14.90
American opportunity tax credit		
\$2,500 credit refundable up to \$1,000	\$6.90	\$75.50
Total Recovery Act Provisions	\$19.90	\$188.70
Double Earned Income Tax Credit for Childless Workers	---	\$29.10

Source: U.S. Department of the Treasury (Feb. 2010), General Explanations of the Administration's Fiscal Year 2011 Revenue Proposals, <http://www.treas.gov/offices/tax-policy/library/greenbk10.pdf> and U.S. Congress, House Committee on Ways and Means, H.R. 3970 Tax Reduction and Reform Act of 2007, Oct. 2007, http://waysandmeans.house.gov/media/pdf/110/Summary_for_Distribution.pdf.

The Statutory Pay-As-You-Go Act of 2010 exempted the ARRA CTC reform and EITC expansion for married filers from the "PAYGO" rules, meaning that these two provisions do not need to be offset by budget cuts or tax increases. As a result, Congress must find offsets for the \$90 billion combined cost of the EITC expansion for families with three or more children and the American Opportunity Tax Credit. Congress would also need to find an additional \$30 billion to offset an increase in the EITC for childless workers.

The cost of extending the Recovery Act provisions pales in comparison to existing tax benefits to the financial industry, multinational corporations as well as gas and oil companies. The President's Fiscal Year 2011 Budget estimates that the federal government could raise as much as \$467 billion by closing existing loopholes, many of which encourage U.S. corporations to ship jobs offshore and shelter profits overseas.²⁵ Others, such as the "carried interest" loophole, put the economy in jeopardy by rewarding Wall Street for taking out-sized risks.

Table 3. Potential Loophole Closers, Fiscal Years 2011 to 2020

	Dollars (billion)
	FY 2011 - FY 2020
End preferential treatment of income for hedge fund managers (carried interest)	\$24
Eliminate preferences for the oil, gas and coal industry	\$39
Reform U.S. international tax system	\$122
Repeal LIFO method of accounting for inventories	\$59
Reform treatment of financial institutions and products	\$93
Total Loophole Closers	\$337

Source: U.S. Department of the Treasury (Feb. 2010), General Explanations of the Administration's Fiscal Year 2011 Revenue Proposals, <http://www.treas.gov/offices/tax-policy/library/greenbk10.pdf>.

Conclusion

By enacting the American Recovery and Reinvestment Act, Congress took swift and bold action to revive the economy. In the process, Congress passed several tax reforms that are now in jeopardy of being eliminated. For moderate-income families and particularly those with young children or college students, literally thousands of dollars are at stake. Working Americans simply cannot afford to lose valuable refundable credits such as the Child Tax Credit, the Earned Income Tax Credit and the American Opportunity Tax Credit. With millions of Americans at risk of losing substantial income supports, failure to act to extend these credits is no longer an option. Making permanent the expansions of the CTC, EITC and educational support of the American Opportunity Tax Credit are necessary to continue to stabilize our nation's financial security now and for future generations. As the current session nears its end, Congress must prioritize efforts to hold low- and moderate-income taxpayers harmless against any tax increases or loss of current tax benefits. Strengthening the supports currently available will place low- and moderate-income families already perched in the most precarious economic positions on firmer financial footholds.

Appendix A: Taxpayer Scenarios

Scenario 1. Head of Household, One Child (under 17)

	2001/2003 Tax Cuts Extended		2001/2003 Tax Cuts Expire
	Recovery Act	Without Recovery Act	
Income	\$12,800	\$12,800	\$12,800
Income Tax Before Credits	\$0	\$0	\$0
Tax Credits			
Child Tax Credit	\$1,000	---	---
Earned Income Credit	\$3,104	\$3,104	\$3,104
Making Work Pay Credit	\$400	---	---
Education Credit	---	---	---
Social Security and Medicare Taxes	(\$979)	(\$979)	(\$979)
Income After Federal Taxes	\$16,325	\$14,925	\$14,925
Difference in After-Tax Income	\$1,400	---	---

Scenario 2. Head of Household, Two Children (under 17)

	2001/2003 Tax Cuts Extended		2001/2003 Tax Cuts Expire
	Recovery Act	Without Recovery Act	
Income	\$20,000	\$20,000	\$20,000
Income Tax Before Credits	\$35	\$35	\$53
Tax Credits			
Child Tax Credit	\$2,000	\$1,115	---
Earned Income Credit	\$4,444	\$4,444	\$4,444
Making Work Pay Credit	\$400	---	---
Education Credit	---	---	---
Social Security and Medicare Taxes	(\$1,530)	(\$1,530)	(\$1,530)
Income After Federal Taxes	\$25,279	\$23,994	\$22,861
Difference in After-Tax Income	\$1,285	---	---

Scenario 3. Married Couple, Three Children (under 17)

	2001/2003 Tax Cuts Extended		2001/2003 Tax Cuts Expire
	Recovery Act	Without Recovery Act	
Income	\$30,000	\$30,000	\$30,000
Income Tax Before Credits	\$0	\$0	\$270
Tax Credits			
Child Tax Credit	\$3,000	\$2,580	\$0
Earned Income Credit	\$4,032	\$3,009	\$2,338
Making Work Pay Credit	\$800	---	---
Education Credit	---	---	---
Social Security and Medicare Taxes	(\$2,295)	(\$2,295)	(\$2,295)
Income After Federal Taxes	\$35,537	\$33,294	\$29,773
Difference in After-Tax Income	\$2,243	---	---

Scenario 4. Married Couple, Three Children (two under 17 and one in college)

	2001/2003 Tax Cuts Extended		2001/2003 Tax Cuts Expire
	Recovery Act	Without Recovery Act	
Income	\$35,000	\$35,000	\$35,000
Income Tax Before Credits	\$490	\$490	\$420 ^a
Tax Credits			
Child Tax Credit	\$2,000	\$2,000	\$420
Earned Income Credit	\$2,979	\$1,956	\$1,285
Making Work Pay Credit	\$800	---	---
Education Credit	\$1,490	\$490	---
Social Security and Medicare Taxes	(\$2,678)	(\$2,678)	(\$2,678)
Income After Federal Taxes	\$39,102	\$36,279	\$33,608
Difference in After-Tax Income	\$2,823	---	---

Scenario 5. Single Worker Earning Minimum Wage

	2001/2003 Tax Cuts Extended		2001/2003 Tax Cuts Expire
	Recovery Act	Without Recovery Act	
Income	\$15,000	\$15,000	\$15,000
Income Tax Before Credits	\$550	\$550	\$825
Tax Credits			
Child Tax Credit	---	---	---
Earned Income Credit	---	---	---
Making Work Pay Credit	\$400	---	---
Education Credit	---	---	---
Social Security and Medicare Taxes	(\$1,148)	(\$1,148)	(\$1,148)
Income After Federal Taxes	\$13,703	\$13,303	\$13,028
Difference in After-Tax Income	\$400	---	---

Scenario 6. Head of Household, Two Children (one under 17 and one in college)

	2001/2003 Tax Cuts Extended		2001/2003 Tax Cuts Expire
	Recovery Act	Without Recovery Act	
Income	\$25,000	\$25,000	\$25,000
Income Tax Before Credits	\$535	\$535	\$203 ^a
Tax Credits			
Child Tax Credit	\$1,000	\$1,000	\$203
Earned Income Credit	\$3,391	\$3,391	\$3,391
Making Work Pay Credit	\$400	---	---
Education Credit	\$1,535	\$535	---
Social Security and Medicare Taxes	(\$1,913)	(\$1,913)	(\$1,913)
Income After Federal Taxes	\$28,879	\$27,479	\$26,479
Difference in After-Tax Income	\$1,400	---	---

Scenario 7. Single Worker and Part-time Student (no children)

	2001/2003 Tax Cuts Extended		2001/2003 Tax Cuts Expire
	Recovery Act	Without Recovery Act	
Income	\$25,000	\$25,000	\$25,000
Income Tax Before Credits	\$1,899	\$1,899	\$2,325
Tax Credits			
Child Tax Credit	---	---	---
Earned Income Credit	---	---	---
Making Work Pay Credit	\$400	---	---
Education Credit	\$2,500	\$1,800	\$1,800
Social Security and Medicare Taxes	(\$1,913)	(\$1,913)	(\$1,913)
Income After Federal Taxes	\$24,089	\$22,989	\$22,563
Difference in After-Tax Income	\$1,100	---	---

* Scenarios assume the household's education expenses were significant enough to qualify for the maximum education tax benefit available at the household's income level. In addition to education credits, there is also a tuition and fees deduction. If the 2001/2003 tax cuts were to expire the family would no longer be eligible for an education tax credit. In this case, the parents would take the tuition and fees deduction, which explains why the family's income tax before credits is lower when the 2001/2003 tax cuts expire.

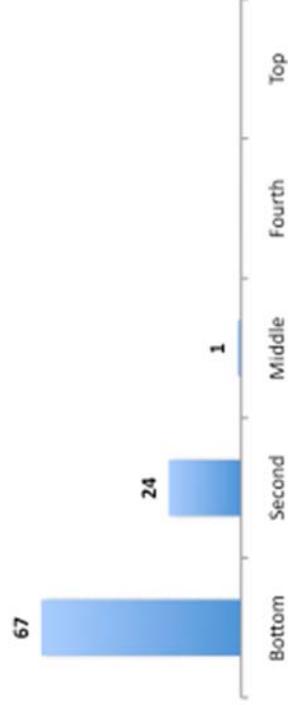
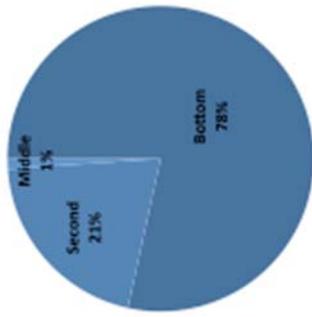
Appendix B: Summary of American Recovery and Reinvestment Act Tax Provisions for Working Families

Refundable Tax Credit	What Changed	Technical Description
Child Tax Credit	Lowered income requirement for the refundable portion of the credit	The credit is refundable up to 15% of earnings in excess of \$3,000 (Without ARRA the earnings threshold would increase to approximately \$12,800)
Earned Income Tax Credit	Added a third tier for families with three or more children	For families with 3 or more children, maximum credit increases from \$5,036 to \$5,666 for 2010 Credit is available up to earned income of \$43,352 for head of household filers and \$48,362 if married filing jointly (would be \$40,363 for head of households and \$45,373 if married filing jointly without new tier)
	Reduced the marriage penalty	Extended the phase out range over head of household and single filers from \$3,120 to \$5,000 (e.g., In 2010, credit is phased out by earnings of \$35,535 for head of households with one child and married taxpayers filing jointly can claim the credit up to earnings of \$40,545)
	Replaced the Hope education credit for 2009 and 2010 (Hope credit was non-refundable, applied to only the first two years of post-secondary education and only covered tuition expenses)	Maximum value of \$2,500 Equals 100% of the first \$2,000, plus 25% of the next \$2,000, of qualified tuition and related expenses (student must be at least half-time) 40% of the credit is refundable (for a maximum refundable credit of \$1,000) Credit is available for 4 years of post-secondary education Covers qualified tuition and related expenses (e.g., books and course supplies) Phases out for taxpayers with adjusted gross income between \$80,000 and \$90,000 (\$160,000 and \$180,000 if married filing jointly)
Making Work Pay Credit	Created a new refundable tax credit available to 95 percent of workers	Maximum value of \$400 for individuals and \$800 for married couples Equals 6.2% of earnings up to \$6,452 for individuals and \$12,903 if married filing jointly Phases out for taxpayers with modified adjusted gross income between \$75,000 and \$95,000 (\$150,000 and \$190,000 if married filing jointly)

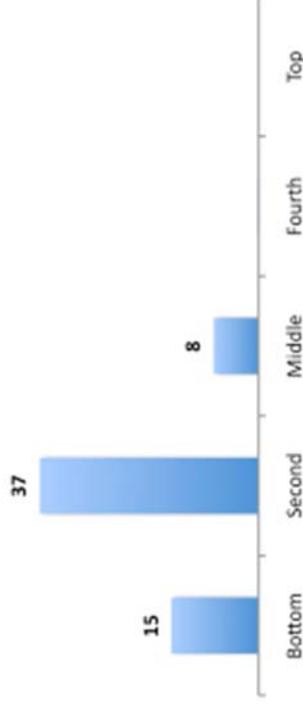
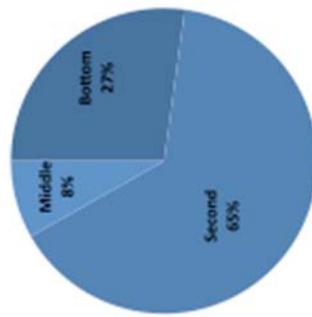
Appendix C: Distribution of Tax Benefits

Distribution of Tax Benefits by Income Quintile

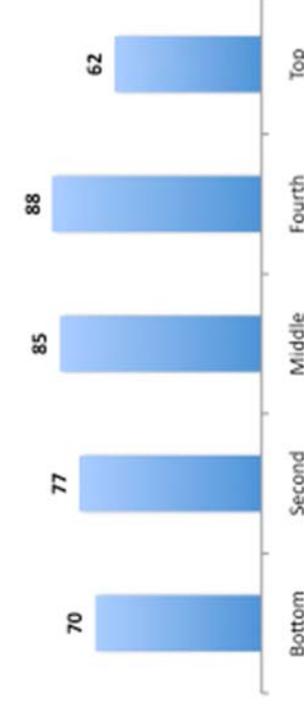
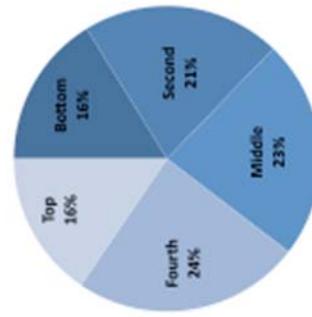
Percentage of Taxpayers Receiving Credit



Child Tax Credit
(impact on families with children)



Earned Income Tax Credit
(impact on families with children of reduced marriage penalty and tier for families with 3 or more children)



Making Work Pay Credit

End Notes

¹Alan S. Blinder and Mark Zandi (2010), How the Great Recession was brought to an end, <http://www.economy.com/mark-zandi/documents/End-of-Great-Recession.pdf>.

²Economic Growth and Tax Relief Reconciliation Act of 2001 (Pub.L. 107-16, 115 Stat. 38, Jun 7, 2001) and Jobs and Growth Tax Relief Reconciliation Act of 2003 (Pub.L. 108-27, 117 Stat. 752, May 23, 2003).

³President Obama's mid-session budget review projected an unemployment rate of 8.7 percent in 2011 and 7.7 percent in 2012. For more information see Office of Management and Budget, Mid-session review budget of the U.S. government, fiscal year 2011, table 2. economic assumptions, <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2011/assets/11msr.pdf>.

⁴U.S. Department of Labor, Bureau of Labor Statistics (Jul. 2010), Employment situation, table A-12, <http://bls.gov/news.release/pdf/empsit.pdf>.

⁵U.S. Department of Labor, Bureau of Labor Statistics (Jul. 2010), Employment situation, summary table A. household data, seasonally adjusted, <http://bls.gov/news.release/pdf/empsit.pdf>.

⁶Christian E. Weller (Aug. 2010), Economic snapshot for 2010, Center for American Progress, http://www.americanprogress.org/issues/2010/08/pdf/aug10_econ_snapshot.pdf.

⁷Weller, Economic snapshot.

⁸Weller, Economic snapshot.

⁹Tamar Lewin, Once a leader, U.S. lags in college degrees," *The New York Times*, 23 Jul. 2010, http://www.nytimes.com/2010/07/23/education/23college.html?_r=1&scp=4&sq=college_education&st=cse.

¹⁰The \$12,850 Child Tax Credit earnings threshold cited in the beginning of this section is an estimate provided by the Center on Budget and Policy Priorities based on predicted inflation. The sample taxpayer scenarios throughout the paper were calculated using the Tax Foundation's online tax calculator, which assumed that the threshold would be \$12,800. This \$50 difference does not have a substantial impact on the calculations.

¹¹Arloc Sherman, Avi Feller and Chuck Marr (Feb. 2010), Failure to extend improvements in the Child Tax Credit would harm millions of low-income working families, Center on Budget and Policy Priorities, <http://www.cbpp.org/files/2-16-10tax2.pdf>.

¹²Amounts given are for Tax Year 2009. Maximum amount and upper income levels will increase in 2010.

¹³Center on Budget and Policy Priorities. Presentation for state groups on refundable tax credits given 29 Mar. 2010, presentation was made available upon request.

¹⁴Center on Budget and Policy Priorities, Presentation for state groups on refundable tax credits.

End Notes (cont.)

¹⁵Center on Budget and Policy Priorities, Presentation for state groups on refundable tax credits.

¹⁶Tax Policy Center (Sep. 2006), Tax benefits of the Hope Credit, Lifetime Learning Credit, deduction for higher education expenses, and student loan interest deduction: by adjusted gross income class, 2005, Table T06-0330, <http://www.taxpolicycenter.org/numbers/displayatab.cfm?Docid=1667&DocTypeID=1>.

¹⁷Chye-Ching Huang, Robert Greenstein, and Gillian Brunet (Feb. 2009), House and Senate recovery packages would improve higher education tax credits, Center on Budget and Policy Priorities, Table 3, <http://www.cbpp.org/files/1-21-09tax2.pdf>.

¹⁸Chye-Ching Huang, et. al., Table 3.

¹⁹Chye-Ching Huang, et. al, 1.

²⁰For an overview of research on the EITC's work incentive see Joseph V. Hotz, and John Karl Scholz (Aug. 2002), The Earned Income Tax Credit, http://www.econ.wisc.edu/~scholz/Research/EITC_Survey.pdf. For research on the future earnings of Earned Income Tax Credit recipients see Molly Dahl, Thomas DeLeire and Jonathan Schwabish (Apr. 2009), Stepping stone or dead end? The effect of the EITC on earnings growth, <http://www.irp.wisc.edu/publications/dps/pdfs/dp136509.pdf>.

²¹For a summary of Earned Income Tax Credit proposals see Table 3 in Alan Berube, David Park and Elizabeth Kneebone (Jun. 2008), Metro raise: Boosting the Earned Income Tax Credit to help metropolitan workers and families, http://www.brookings.edu/~media/Files/rc/reports/2008/05_metro_raise_berube/metroraise_report.pdf.

²²Source: Joint Committee on Taxation (Oct. 2008), Estimates of federal tax expenditures for fiscal years 2008–2012, <http://www.jct.gov/publications.html?func=startdown&id=1192>.

²³For more information see United States Department of Treasury (Jun. 2009), General explanations of the administration's fiscal year 2010 revenue proposal, <http://www.treas.gov/offices/tax-policy/library/grnbk09.pdf> and David Neville, The Saver's Bonus encouraging and facilitating savings by working families at tax time, New America Foundation, http://www.newamerica.net/files/nafmigration/Savers_Bonus_Two_Pager_FINAL_070209.pdf.

²⁴The \$30 billion estimate is based on 2007 legislation (H.R. 3970) that would have doubled the EITC percentage from 7.65 percent to 15.3 percent (essentially doubling the credit's maximum value) for childless workers. The budgeted amount could change depending on the actual chosen parameters (e.g., when the credit begins phasing out). For more information on H.R. 3970 see a summary of the bill at U.S. Congress, House Committee on Ways and Means (Oct. 2007), H.R. 3970 Tax Reduction and Reform Act of 2007, http://waysandmeans.house.gov/media/pdf/110/Summary_for_Distribution.pdf.

²⁵Robert S. McIntyre, Multinational Corporate Tax Abuses and Proposed Solutions, summary of remarks at a 24 Jul. 2010 Congressional briefing, <http://www.ctj.org/pdf/summaryremarksoffshorecorpabuses.pdf>.



National Community Tax Coalition
29 E. Madison Street, Suite 900
Chicago, IL 60602
(312) 252-0280

www.tax-coalition.org