

PAYCHECK \$ and POLITICS

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A State EITC for Arkansas's Working Families: Giving Credit Where It's Long Overdue

By Ginny Blankenship

Summary

- In these uncertain economic times, Arkansas's hard-working families are having trouble making ends meet. They need help, and a state earned income tax credit, or EITC, could make a real difference.
- A state EITC based on the federal version, combined with the further reduction or elimination of the sales tax on food, would help balance the regressive nature of state and local sales taxes and create a fairer state tax system in Arkansas.
- A refundable EITC is a proven method of putting more money back in the hands of those who need it most, while at the same time encouraging them to stay in the workforce. It does this by giving a tax credit to certain workers and refunding them the difference between the credit and any paid income tax.
- The federal EITC has been so successful in reducing poverty that over half of all states with personal income taxes have adopted state-level EITCs based on it.
- One quarter of all Arkansas families filing federal tax returns benefited from the federal EITC in 2005, returning an average of \$2,016 to their pockets.
- AACF estimates that it would cost approx. \$56 million for Arkansas to implement a state EITC equal to 10 percent of the federal EITC beginning in FY 2009, or \$113 million for a state EITC equal to 20 percent of the federal EITC.
- Research shows that working families use the EITC refund to pay off debt, finance transportation to work, invest in education, and buy basic necessities—all of which have an impact on local communities. The federal EITC alone puts over half a billion dollars into Arkansas's economy each year.

Introduction

Economic trends in Arkansas have made it harder for many families to make ends meet despite having one or even two working parents. To make matters worse, working families have long paid an unfair share of the tax burden in our state.¹ A state earned income tax credit (EITC), modeled on the federal EITC currently in place, could help these families keep more money in their pocket, which can help them build a stronger future, while at the same time putting more money back into local communities. In these tough economic times, a state EITC, combined with the elimination of the sales tax on food, will directly improve the economic well-being of families and give them hope for the future.

What is an EITC?

State EITCs are generally based on the existing federal EITC, which was designed to help low- and moderate-income working families make ends meet and serve as an incentive for these families to join or stay in the workforce. Enacted in 1975 under President Ford, and expanded under Presidents Reagan, Bush and Clinton, the federal EITC is a refundable tax credit that can be claimed by working families meeting certain criteria. It's a policy that is supported by officials on both sides of the aisle. President Reagan even called the EITC the "best anti-poverty, the best pro-family, the best job creation measure to come out of Congress."²

Working families with incomes of up to \$35,241 with one child and up to \$39,783 with two or more children currently qualify for the federal EITC, which is the same threshold for a state EITC. Most Arkansas families (69 percent) receiving the federal EITC earn less

than \$20,000 per year; those with incomes between \$11,750 and \$17,400 benefit the most. The chart on page three illustrates who qualified for the federal EITC as of 2007, and the average tax credit that they received.³

The federal EITC has been so successful in reducing poverty that 24 of the 42 states with personal income taxes (including the District of Columbia) have adopted state-level EITCs based on the federal EITC (see Table 2). In fact, two southern states, Louisiana and North Carolina, recently jumped ahead of Arkansas in creating state EITCs. The most recent state to adopt a credit was Washington state in early April.

Twenty-one states follow the federal practice of making the credit "refundable," meaning that if the credit exceeds the family's income tax liability, the balance of the credit is returned to the family in a refund check.

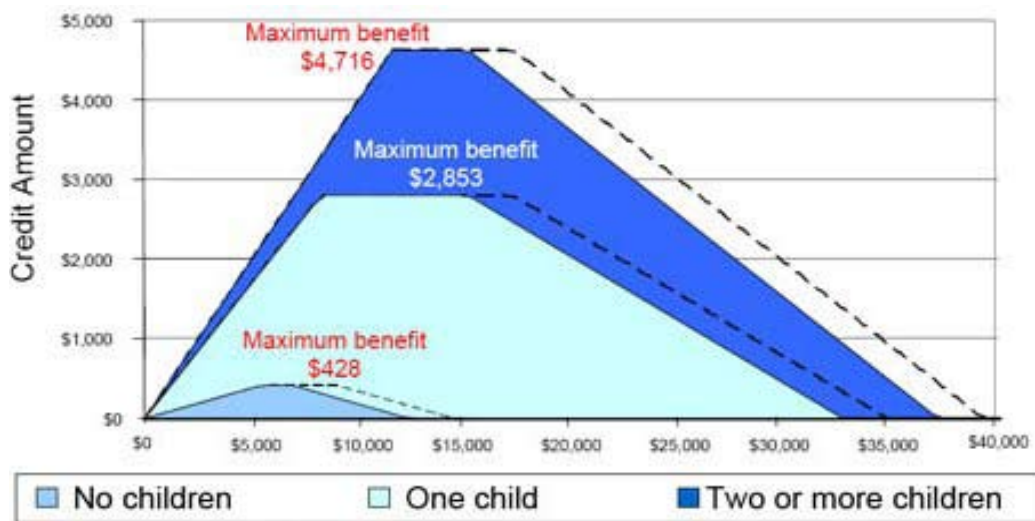
The EITC Works for Working Families

State EITCs have proven to be a highly effective strategy for reducing poverty in other states:

- The National Center for Children in Poverty found that the federal EITC reduces child poverty for young children by nearly 25 percent—more than any other government program. State EITCs compound these benefits by building on the federal program.
- Research shows that working families use the EITC refund to pay off debt, finance transportation to work, invest in education, and buy basic necessities—nearly all of which stays in local communities.

- Many working families also use their EITC refund to begin building assets and creating long-term wealth—an important step toward breaking the cycle of poverty from generation to generation.
- One quarter of all Arkansas families filing federal tax returns benefited from the federal EITC in 2005, returning an average of \$2,016 to their pockets—and over half a billion dollars to the state’s economy (see Table 1).⁴ Enacting a 10 percent state EITC would bring an additional \$50 million to Arkansas communities.
- Families in all 75 counties in Arkansas claim the credit. Phillips County had the highest participation and the highest average credit: almost half (48 percent) got an average of \$2,442. Saline County had the lowest participation (17 percent), while Carroll County had the lowest average credit (\$1,811).

Working Families Qualifying for the Federal EITC in 2007



Note: Married couples with incomes in the phase-out range qualify for a higher credit than single parents as shown by lined dashes.

Source: Center on Budget & Policy Priorities

Table 1 shows the number of federal tax return filers in Arkansas that claimed for the federal EITC in tax year 2005 (the most recent year available), as well as the average tax credit they received and the total amount of federal EITC funding received in each county. Note that these figures do not reflect

Table 1: Federal EITC Usage by Arkansas Counties in 2005

County	Total # Tax Returns Filed	# Returns Claiming EITC	% Returns Claiming EITC	Total Amount EITC \$	Average EITC \$ Per Filer
Arkansas	8,498	2,317	27%	\$4,583,138	\$1,978
Ashley	8,571	2,571	30%	\$5,397,391	\$2,099
Baxter	17,532	3,315	19%	\$6,049,545	\$1,825
Benton	78,797	13,470	17%	\$25,926,787	\$1,925
Boone	14,651	3,296	22%	\$6,048,000	\$1,835
Bradley	4,295	1,318	31%	\$2,808,110	\$2,131
Calhoun	1,738	496	29%	\$998,643	\$2,013
Carroll	10,740	2,756	26%	\$4,989,537	\$1,811
Chicot	4,509	1,961	43%	\$4,522,788	\$2,307
Clark	8,958	2,368	26%	\$4,774,822	\$2,017
Clay	6,441	1,676	26%	\$3,087,066	\$1,842
Cleburne	10,409	2,198	21%	\$4,186,546	\$1,905
Cleveland	3,214	783	24%	\$1,618,148	\$2,067
Columbia	9,819	2,881	29%	\$5,821,284	\$2,020
Conway	8,034	2,045	25%	\$4,052,844	\$1,982
Craighead	35,050	8,228	23%	\$16,275,920	\$1,978
Crawford	22,860	5,633	25%	\$11,390,669	\$2,022
Crittenden	20,179	7,806	39%	\$18,013,704	\$2,308
Cross	7,327	2,373	32%	\$4,993,253	\$2,104
Dallas	3,217	1,051	33%	\$2,311,194	\$2,199
Desha	5,476	2,161	39%	\$4,621,459	\$2,139
Drew	7,067	2,146	30%	\$4,592,738	\$2,140
Faulkner	40,086	7,767	19%	\$14,869,213	\$1,914
Franklin	6,942	1,644	24%	\$3,174,634	\$1,931
Fulton	4,014	1,087	27%	\$2,039,961	\$1,877
Garland	40,246	8,778	22%	\$16,761,939	\$1,910
Grant	6,620	1,307	20%	\$2,492,027	\$1,907
Greene	15,679	3,724	24%	\$6,880,261	\$1,847
Hempstead	8,761	3,134	36%	\$6,891,345	\$2,199
Hot Spring	12,031	2,996	25%	\$5,757,120	\$1,922
Howard	5,728	1,767	31%	\$3,635,847	\$2,058
Independence	14,010	3,383	24%	\$6,397,735	\$1,891
Izard	4,658	1,177	25%	\$2,150,562	\$1,828
Jackson	6,364	1,949	31%	\$3,869,160	\$1,986
Jefferson	31,748	10,833	34%	\$23,568,548	\$2,176
Johnson	8,866	2,501	28%	\$5,034,418	\$2,013
Lafayette	2,521	950	38%	\$1,986,135	\$2,090
Lawrence	6,576	1,893	29%	\$3,665,652	\$1,936

the overall EITC take-up rate; data is not available on the total number of individuals eligible for the federal EITC in each county in Arkansas. In other words, actual utilization rates may be much higher.

Table 1: Federal EITC Usage by Arkansas Counties in 2005

County	Total # Tax Returns Filed	# Returns Claiming EITC	% Returns Claiming EITC	Total Amount EITC \$	Average EITC \$ Per Filer
Lee	3,277	1,458	44%	\$3,340,294	\$2,291
Little River	5,195	1,397	27%	\$2,877,383	\$2,060
Logan	8,805	2,199	25%	\$4,327,040	\$1,968
Lonoke	25,319	5,321	21%	\$10,319,499	\$1,939
Madison	5,468	1,304	24%	\$2,542,651	\$1,950
Marion	6,263	1,488	24%	\$2,801,333	\$1,883
Miller	16,598	4,783	29%	\$10,159,639	\$2,124
Mississippi	17,812	6,752	38%	\$15,214,223	\$2,253
Monroe	3,514	1,352	38%	\$2,958,551	\$2,188
Montgomery	2,966	709	24%	\$1,398,738	\$1,972
Nevada	3,597	1,180	33%	\$2,410,424	\$2,043
Newton	2,894	861	30%	\$1,632,243	\$1,897
Ouachita	10,838	3,376	31%	\$6,909,737	\$2,047
Perry	4,143	972	23%	\$1,954,284	\$2,011
Phillips	8,287	3,994	48%	\$9,753,874	\$2,442
Pike	3,821	977	26%	\$1,836,524	\$1,880
Poinsett	9,276	2,992	32%	\$6,210,700	\$2,076
Polk	7,420	2,199	30%	\$4,357,560	\$1,982
Pope	23,657	5,560	24%	\$10,571,049	\$1,901
Prairie	3,243	861	27%	\$1,701,273	\$1,976
Pulaski	165,940	38,311	23%	\$77,839,383	\$2,032
Randolph	6,607	1,800	27%	\$3,581,915	\$1,990
St. Francis	9,572	4,069	43%	\$9,614,429	\$2,363
Saline	40,153	6,825	17%	\$12,983,313	\$1,902
Scott	3,881	1,228	32%	\$2,581,637	\$2,102
Searcy	2,967	915	31%	\$1,675,303	\$1,831
Sebastian	49,790	12,062	24%	\$23,662,180	\$1,962
Sevier	5,588	1,738	31%	\$3,772,195	\$2,170
Sharp	6,983	1,918	27%	\$3,677,176	\$1,918
Stone	4,164	1,188	29%	\$2,252,168	\$1,896
Union	17,777	5,204	29%	\$10,745,831	\$2,065
Van Buren	5,948	1,451	24%	\$2,807,553	\$1,934
Washington	76,759	15,136	20%	\$28,522,715	\$1,884
White	27,506	6,603	24%	\$12,921,092	\$1,957
Woodruff	2,959	1,123	38%	\$2,365,100	\$2,105
Yell	8,288	2,439	29%	\$4,952,121	\$2,030
TOTAL	1,123,423	280,768	25%	\$566,115,452	\$2,016

Source: The Brookings Institution's EITC Project, February 2008

Table 2: States with Earned Income Tax Credits

State	Year Enacted	Refundable?	% of Federal EITC
Delaware	2005	No	20%
District of Columbia	2000	Yes	35%
Illinois	2000	Yes	5%
Indiana	1999	Yes	9%
Iowa	1989	Yes	7%
Kansas	1998	Yes	17%
Louisiana	2007	Yes	3.5%
Maine	2000	No	5%
Maryland	1987	Yes	50% of federal EITC non-refundable, 25% refundable
Massachusetts	1997	Yes	15%
Michigan	2006	Yes	10% in 2008; 20% beginning in 2009
Minnesota	1991/92, 1997/98 restructured	Yes	Varies based on income, # children, etc.; Average: 33%
Nebraska	2006	Yes	10%
New Jersey	2000	Yes	22.5% in 2008; 25% beginning in 2009
New Mexico	2007	Yes	8%
New York	1994	Yes	30%
North Carolina	2007	Yes	3.5%
Oklahoma	2002	Yes	5%
Oregon	1997	Yes	6% in 2008
Rhode Island	1986	Yes, 10%	25%
Vermont	1988	Yes	32%
Virginia	2004	No	20%
Wisconsin	1989	Yes	4% of federal for 1 child, 14% for 2 children, 43% for 3 or more children
Washington	2008	Yes	5% in 2009-2010; 10% beginning in 2011

Source: www.StateEITC.com;
Center on Budget & Policy Priorities

How Would A State EITC Work in Arkansas?

A state EITC would provide tax relief to hard-working, low-income families in Arkansas, helping them close the gap between what they earn and what they need to make ends meet. A state EITC in Arkansas would simply piggyback on the federal EITC and would require adding only one line to the state income tax form to implement the credit. Two features would be critical to a successful state EITC:

1. It should be refundable so that any credit over the state income tax owed is returned to the family as a reward for working hard at low-paying jobs.
2. It should be set at a percentage of the federal EITC to help make it easy to administer (usually 10-50 percent in other states).

AACF estimates that it would cost approximately \$56 million for Arkansas to implement a state EITC equal to 10 percent of the federal EITC beginning in FY 2009, or \$113 million for a state EITC equal to 20 percent of the federal EITC—\$15 million less than the recent 3 percent cut of the grocery tax.⁵

No matter what percentage the state chose to implement, a state EITC would have very low administrative costs, typically much less than one percent of the cost of the credit. Because the federal government invests heavily in enforcement and keeps a comprehensive database to track EITC eligibility, the state can piggyback on these efforts.

In summary, a state EITC, in tandem with the further reduction or elimination of the state sales tax on food, would provide a critical financial boost to working families who need help most while at the same time putting millions of dollars back into Arkansas's local communities.



Notes:

1. Arkansas Advocates for Children & Families (AACF), "Tax Relief for Low-Income Arkansans: What are the Options?", January 2007.

2. President Ronald Reagan, "Sweeping Tax Overhaul Now the Law," *Chicago Tribune*, October 23, 1986.

3. Center on Budget & Policy Priorities (CBPP), "A Majority Of States With Income Taxes Have Enacted State Earned Income Tax Credits," October 5, 2007, <http://www.cbpp.org/10-5-07sfp.htm>

4. AACF calculations of the latest available IRS data from the Brookings Institution's EITC Project. Prior data available online: <http://www.brookings.edu/metro/EITC/EITC-Homepage.aspx>

5. AACF calculations are based on data from the IRS and the U.S. Office of Management and Budget, using methodology from the CBPP: "How Much Would a State Earned Income Tax Credit Cost in 2009?" March 5, 2008, <http://www.cbpp.org/3-5-08sfp.htm>. Estimates are adjusted to account for eligible non-users and only apply to credits that are refundable and that are set at a flat percent of the federal EITC.

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