

Claiming Full Credit

Strengthening Virginia's Working Families



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Like many other states, Virginia has a powerful and proven tool for strengthening the commonwealth's communities, and boosting its economy. But this tool – the Earned Income Credit (EIC) – could do a better job with one fairly simple change.

This change would help low-wage working families, including thousands serving in the military, to keep more of their earnings to pay for necessities like housing, food, transportation, and childcare – basics that eat up a greater share of their income than in wealthier households.

To bring Virginia's EIC to its full potential as a tool to help low-income working families, it should be made refundable.

What That Means

Virginia's EIC is rooted in the federal Earned Income Tax Credit (EITC) created in 1975. As one of the largest and most effective ways to combat poverty in the United States, the federal EITC reduces the taxes paid by low-income, working Americans based on their earnings and the size of their family.

- In 2010, more than 27.5 million middle class and low-income working families received the federal EITC.
- The federal EITC keeps over 6.5 million Americans, **more than half of them children**, out of poverty each year.

Virginia launched the state EIC in 2006. Like the federal program, it goes to those eligible in the form of a credit against their taxes. At the federal level if a family's income is so low they don't actually owe taxes, they get their share of the tax credit as cash – in essence, a refund. If that sounds like a giveaway, it isn't. It just recognizes that, even though they owe no federal income taxes, these families still pay payroll and other federal taxes, like the federal gas tax, that take a larger share of their income than the wealthiest households.

The Virginia credit equals up to 20 percent of their federal EITC to help offset state and local taxes. However, unlike the federal program, Virginia's credit is not refundable

when a family's tax liability is lower than the full amount of the credit. Making Virginia's credit refundable would go a long way to helping hard working Virginia families make ends meet.

Why Virginia's EIC Helps Workers

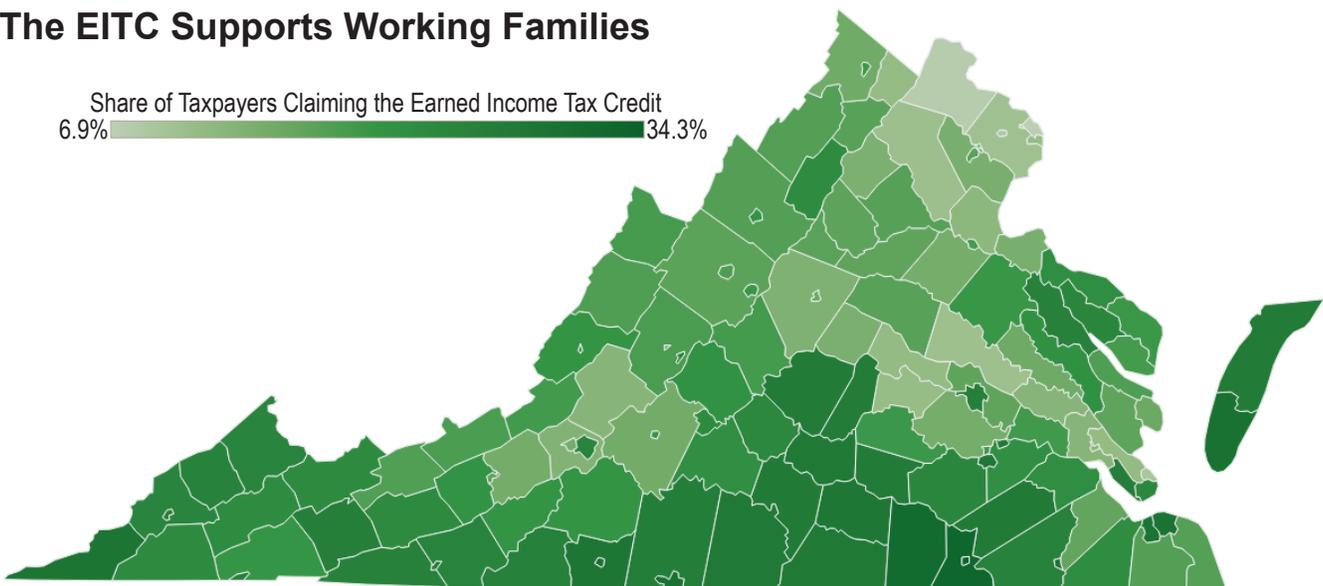
Virginia's EIC is Good for Workers and Business

Virginia's EIC provides targeted help to low-income working families and frees up their household budgets to pay for basic goods and services they need, like transportation, utility bills, and supplies for their children. This keeps dollars flowing through Virginia's local economies and maintains (or even boosts) consumer demand, which makes the state credit good for both business and workers.

- In 2011, over half a million Virginians were eligible to claim Virginia's EIC.
- Eligible recipients are spread across the state.
- Families in all 134 counties and cities claim the credit.

The EITC Supports Working Families

Share of Taxpayers Claiming the Earned Income Tax Credit
6.9% ————— 34.3%



Virginia's EIC rewards work

- In order to get the credit, you have to have income from working.
- The more a family earns, the bigger the size of the credit up to a maximum amount. As income rises beyond the maximum, the amount of the credit is capped and then slowly phased-out for each additional dollar earned.
- Because the credit helps working families pay for basic things that help make work possible, like transportation and childcare, it enjoys support from business.

Strengthening Virginia's Credit

The Virginia state EIC offers a modest credit for working families of 20 percent of the federal credit, but unlike the federal credit and the credits of many states, it's not refundable. If it were, Virginia's credit would do more to offset the disproportionate impact Virginia's state and local taxes have on hard-working, low-paid families trying to make ends meet.

Virginia's tax system is skewed.

- The lowest-income households pay about 9 percent of their income in state and local taxes – like sales tax, and payroll taxes including Social Security and Medicare.
- The highest income households pay only about 5 percent of their income in state and local taxes.

The historic transportation bill passed during the 2013 legislative session made this worse.

- The sales tax increases included in the package fall more heavily on lower-income families.
- Sales taxes are not based on anyone's ability to pay, unlike income taxes whose rates can rise along with income. Low-income families spend most or all of their earnings on goods subject to the higher taxes.

Making Virginia's EIC refundable would allow families to get the full credit they qualify for after covering their income tax liability.

- Workers who qualify for the credit, generally those in low-wage jobs, would get a tax refund if their credit is greater than the income tax they owe.
- This would help offset a portion of the other taxes they pay, including the higher sales tax in the transportation package.

The refundable provision in the federal EITC helps make low-wage work more viable and reduces poverty and its long-term effects on children.

- The refundable federal credit was the most important factor in the increase in single mothers able to work in the 1990s, research shows.

- The federal credit encouraged half a million families across the country to leave cash welfare for employment in the 1990s.
- Between 2009 and 2011, the federal EITC and the Child Tax Credit, another credit helping low-income families offset the cost of raising kids, helped lift 160,000 Virginians and 85,000 children out of poverty by helping workers and families make ends meet.
- Children living in families that receive these tax credits do better in school, avoid many of the disabilities associated with childhood poverty, and earn higher incomes in adulthood compared to low-income non-recipients.

People who work hard should be able to support their families and stay out of poverty. Making the state EIC refundable would be a key improvement to making sure that people who are willing to work are able to make ends meet. It's a small change that would help a lot of Virginians.

Virginia's Earned Income Credit is a proven and powerful tool for strengthening the commonwealth's communities, and boosting its economy. But it can do better.

The Commonwealth Institute

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