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More Information: Don Baylor, baylor@cppp.org

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EITC 101

First enacted in 1975 under President Ford, the Earned Income Tax Credit, or EITC, is a federal tax credit designed to "make work pay" by providing low- and moderate-income working families with a credit on their earned income. President Reagan called the EITC "the best anti-poverty, the best pro-family, the best job creation measure to come out of Congress." Every year, the EITC lifts over 450,000 Texans—including 250,000 children—out of poverty while pumping billions of dollars into the economy. In Texas, the average EITC refund is \$2,050.

WHO QUALIFIES?

Nearly 24% of all Texas tax filers (over two million people) claimed the Earned Income Tax Credit (EITC) in Tax Year 2004, generating nearly \$4.5 billion in refunds.

Workers who earned up to \$38,348 in 2006 may be eligible, depending on family size:

Who Qualifies for the EITC?

- Workers who were raising one child in their home and had income less than \$32,001 (or \$34,001 for married workers) in 2006 can get an EITC of up to \$2,747;
- Workers who were raising more than one child in their home and had income of less than \$36,348 (or \$38,348 for married workers) in 2006 can get an EITC of up to \$4,536;
- Workers who were not raising children in their home, were between ages 25 and 64 on December 31, 2006, and had income below \$12,120 (or \$14,120 for married workers) can get an EITC up to \$412.

To determine EITC eligibility, families can visit <http://www.irs.gov/pub/irs-pdf/p3524.pdf> (available in English and Spanish) or <http://www.cbpp.org/eic2007/>.

EITC BARRIERS

Lack of awareness. Although more Texans claim the EITC each year, not everyone who is eligible for EITC knows about the refund. For example, 22.2% of eligible tax filers—582,422 workers—did not claim their refunds in 2003. As a result, these Texans (and the economy) lost out on \$1.2 billion.

High-Cost Tax Loan Products. Not everyone who claims the EITC receives the full benefit. This is because thousands turn to Refund Anticipation Loans (RALs) and “holiday” or “pay stub” loans to secure their expected refunds in advance. The catch is that these loans come with hefty fees.

- RALs are high-cost loans offered by commercial tax preparers that cost the filer an average of \$100 to \$250 in fees and tax preparation. Nearly 36% of EITC filers in Texas (about 1.2 million filers) used a Refund Anticipation Loan to claim their EITC in Tax Year 2004.
- “Holiday” or “Pay Stub” loans do not require IRS W-2 documentation, and are much riskier for filers. These products can siphon 10-15% from a filer’s refund with interest rates approaching 170% APR.

FREE EITC SERVICES

The IRS provides two free services to help filers get their money faster.

- VITA (Volunteer Income Tax Assistance) is a volunteer-run tax preparation program which helps tens of thousands of Texans file their taxes free of charge. Tax filers who file electronically through VITA can receive their EITC refund within a week. Filers can locate their nearest VITA site by calling 211.
- “Free File” (<http://www.irs.gov/efile/article/0,,id=118986,00.html>) is an IRS-operated website which allows filers who earn \$52,000 or less to file for free on the internet.

LEGISLATION ON THE TABLE

This legislative session, two bills have been introduced related to the EITC. Both bills would be good for Texas because they would protect working families from high-cost loans, encourage the development of free tax preparation sites, and stimulate the economy.

- HB 1344/SB 1905 would establish registration and disclosure requirements for companies that offer RALs.
- HB 1948/SB 1830 would establish a grant program for entities that offer free tax preparation through the VITA program.

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