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HOUSE OF REPRESENTATIVES
COMMONWEALTH *of* PENNSYLVANIA

House Democratic Policy Committee Hearing

Propel PA – Earned Income Tax Credit & Childcare Tax Credit
Tuesday, February 15, 2022 | 12:00 p.m.
G-50 Irvis Office Building and Virtual
Representative Melissa Shusterman

12:00 p.m.	Dr. Laura Crispin Associate Professor, *Department of Economics* Program Director, *Undergraduate and Graduate Public Policy* *Saint Joseph's University*
	Q & A with Legislators
12:30 p.m.	Kristen Rotz, President *United Way of PA*
	Phil Falvo, Public Policy Director *United Way of PA*
	Q & A with Legislators

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HOUSE OF REPRESENTATIVES
COMMONWEALTH of PENNSYLVANIA

Testimony of Dr. Laura M. Crispin[1]

On PropelPA: EITC and Child and Dependent Care Tax Credits

Before the Pennsylvania House

Democratic Policy Committee

February 15, 2022

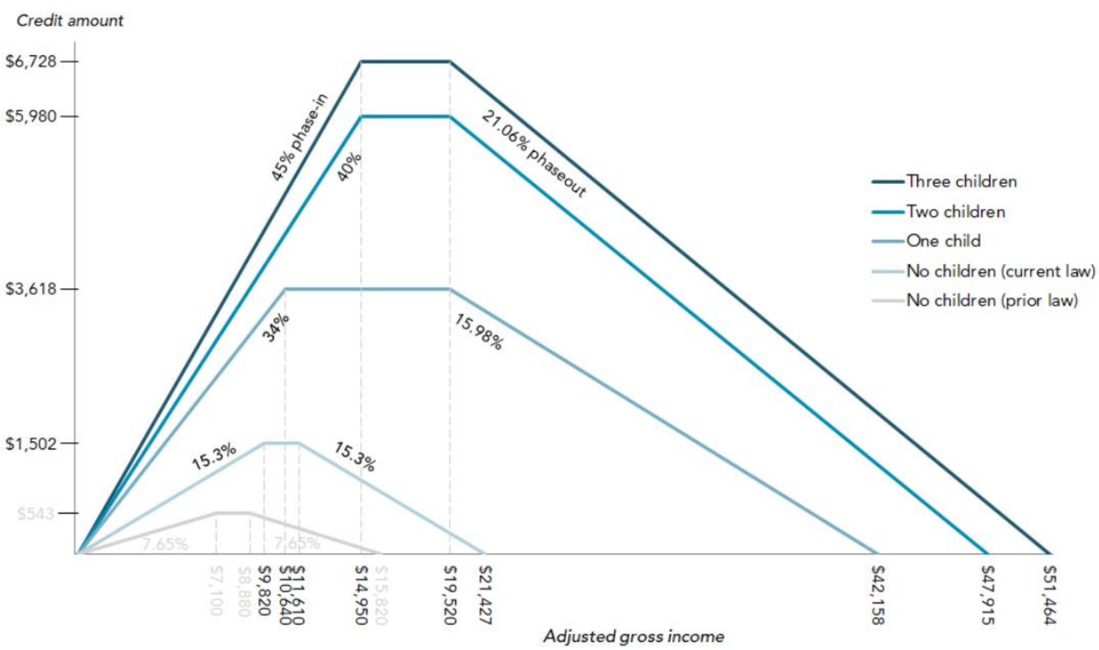
[1] Contact information: lcrispin@sju.edu; (610) 660-1594 (office). Thank you to Tayler Washington for her excellent research assistance.

Earned Income Tax Credit (EITC)

Background

At the federal level, the Earned Income Tax Credit (EITC) has been successful as a policy intervention to support low-wage workers, particularly those with children, while incentivizing labor force participation and full-time employment. As of December 2021, 25 million workers and families received EITC, totaling nearly $60 billion in EITC, with the average EITC received of $2,411.[2]

FIGURE 1
Earned Income Tax Credit
2021



Source: Urban-Brookings Tax Policy Center (2021); Internal Revenue Procedure 2020-45, Internal Revenue Service; and H.R. 1319, "American Rescue Plan Act of 2021," 117th Cong. (2021.)
Notes: Assumes all income comes from earnings. Amounts are for taxpayers filing a single or head-of-household tax return. For married couples filing a joint tax return, the credit begins to phase out at income $5,940 higher than shown, or $5,950 if the couple has children.

The figure above[3] provides a graphical illustration of the phase-in, plateau, and phase-out of benefits for a single worker with no children, one, two, or three children. As an example, the highest amount of credit accrues to a worker with three children, receiving a maximum federal EITC of $6,728 when earning $14,950 in earnings (equivalent to a minimum wage worker earning $7.25 per hour working approximately 40 hours per week for 52 weeks), bringing their total income to $21,678.[4] For reference, the 2021 federal poverty threshold for a one adult-three

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[2] https://www.eitc.irs.gov/eitc-central/statistics-for-tax-returns-with-eitc/statistics-for-tax-returns-with-the-earned-income

[3] https://www.taxpolicycenter.org/briefing-book/what-earned-income-tax-credit

[4] Assuming no tax liability and a fully refundable tax credit.

child household is $27,575,[5] so this household would remain below the poverty threshold while working full-time and receiving the maximum credit.

Once the worker has reached the maximum credit at 45% of their income, there is a plateau in credit, where an increase in income neither increases nor decreases EITC. At the highest income in this range, $19,520, a worker working full-time, full-year would be earning approximately $9.38/hour and with their EITC benefits, would have income of $26,248, which remains below the federal poverty threshold.[6] Beyond this point, EITC begins to phase out at 21.06% as income increases, and ultimately, when the worker earns $51,464, they are no longer eligible for federal EITC credit.

More details about EITC qualifications and thresholds can be found in the recent Congressional Research Report (Crandall-Hollick and Falk, 2020).

Application to EITC proposal for Pennsylvania

As proposed, the PA EITC would be set at 30% of the federal level. Continuing with the earlier example, the worker would receive a maximum state EITC credit of $2,018, bringing their total income (including refundable credit) to $23,696. If the worker were at the highest income level before the phase-out and assuming no taxes owed, their total income including federal and state EITC would be $28,266, which is above the federal poverty threshold.

There are currently 834,000 Pennsylvanians receiving federal EITC credit totaling $1.9 billion, with an average credit of $2,251.[7] This suggests that the total cost of the PA EITC program would be approximately 30% of federal spending on PA EITC recipients, or $570 million, with average state EITC benefits of $675. However, as Neumark and Williams (2020) find, state EITC programs are associated with an increase in federal EITC participation, likely due to the increase in benefits, but also due to a reduction in learning costs for the federal program. This suggests that if enacted in Pennsylvania, there may be an increase in participation and therefore, increase in cost of the state EITC program.

To compare with several neighboring states,[8] Delaware enacted their EITC program in 2005 with non-refundable credit at 20% of the federal EITC level; New Jersey enacted their EITC program in 2000 with refundable credit at 37% of the federal EITC level; Maryland enacted their EITC program in 1987 with refundable credit at 28% of the federal level and non-refundable credit at 50% of the federal level; Ohio enacted their EITC program in 2013 with non-refundable credit at 10% of the federal level.

Research on EITC

[5] https://www.census.gov/data/tables/time-series/demo/income-poverty/historical-poverty-thresholds.html
[6] Still assuming no tax liability and fully refundable EITC.
[7] https://www.eitc.irs.gov/eitc-central/statistics-for-tax-returns-with-eitc/statistics-for-tax-returns-with-the-earned-income
[8] More details for each of these programs and a list of additional states can be found at https://tcwf.wpengine.com/state-tax-credits/

Researchers have acknowledged EITC as one of the most successful anti-poverty programs enacted in the U.S., bringing millions of working adults and their children out of poverty (Schanzenbach and Strain, 2021). A comprehensive review of the literature studying the effects of EITC are provided in Hoynes and Rothstein (2017), and Hoynes and Patel (2018), among others. As these authors summarize, there is significant evidence that EITC incentivizes labor force participation for low-wage workers, pulling those who are not working into the labor force either full- or part-time, particularly among single mothers. There is also some evidence that those working increase their work hours in response to EITC benefits, particularly along the phase-in region of the EITC schedule. The net effect of the employment increases, combined with EITC benefits, is to increase disposable income for low-income workers, decreasing the share in poverty by 8.4 percentage points for every $1000 in federal EITC benefits (Hoynes and Patel, 2018). Hoynes and Rothstein (2017) state that in 2014, EITC and Child Tax Credit (CTC) raised 9.8 million people out of poverty, of that, 5.2 million children.

In addition to labor market participation and increases in income, EITC has been shown to increase infant and maternal health, children's cognitive outcomes, and educational attainment (see Hoynes and Rothstein (2017) for a summary of this literature). Therefore, workers receiving EITC will benefit directly through the increase in income, but there are significant non-monetary benefits to health and human capital for themselves and their children, which will have longer-run effects on the local economy. Furthermore, qualitative research has shown that low-income individuals often spend EITC-related tax refunds on durable goods such as cars and furniture, and only a small share add to their savings (Romich and Weisner, 2000). This increase in spending particularly benefits local economies (Berube, 2006).

Considerations regarding EITC

No policy is without potential drawbacks, EITC included. The key limitation is that the benefits are received as a lump-sum tax refund after tax returns are filed, so eligible workers will not receive their EITC benefits until the following year. This may be problematic for low-wage workers who are credit constrained and need access to these funds with more immediacy (Hoynes and Rothstein, 2017). Furthermore, uptake may not be 100%, as there may be confusion about qualifications or filing. Relatedly, uptake of EITC may lag behind policy implementation, such that benefits to workers, their families, and the economy may not be seen immediately.

Another consideration is that as income increases, workers may become ineligible for other programs such as SNAP (though EITC payments are not included as income for eligibility requirements (Crandall-Hollick and Falk, 2020)). Therefore, while workers may gain benefits from EITC, they may also lose other benefits. Depending on the magnitudes, this could lead to a net negative outcome for those workers.

Finally, related to pandemic recovery, many workers had labor market disruptions in 2020 and 2021, with high levels of unemployment and changes in work hours. As policymakers consider ways to draw workers into the labor market using policies such as EITC, it is worth considering how the pandemic labor market may have negatively affected low-wage workers and reduced their EITC benefits when working fewer hours (or not at all) than desired.[9]

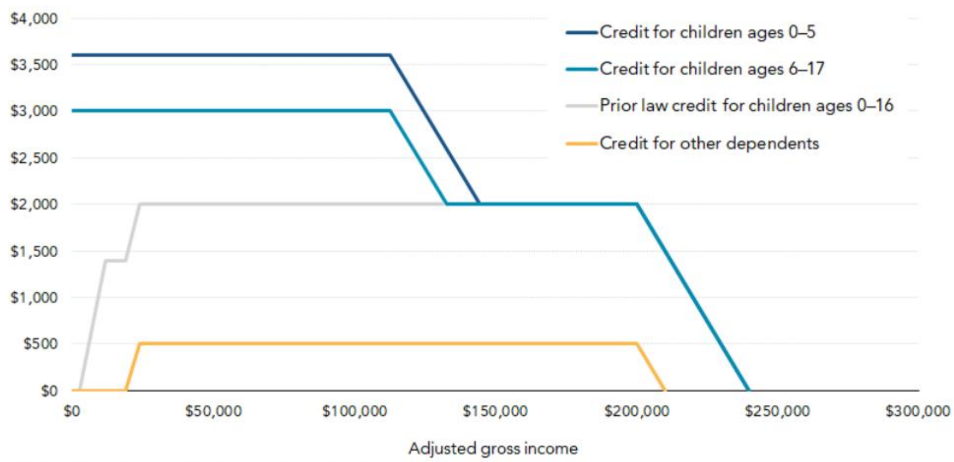
Child Tax Credit (CTC)

Mechanics of CTC

Enacted in 1997, the federal CTC is a less targeted program than EITC, offering tax credits of $2,000 per qualifying child (under 17) to qualifying households (income between $2,000 and $400,000, depending on household composition).[10] In 2021, with the passing of the American Recovery Plan, the CTC amount temporarily increased to $3,000 per child for children 7 to 17 years, and $3,600 for children under 6 years old and became fully refundable.[11]

Like the EITC, there are phase-in, plateau, and phase-out ranges that depend on the number of adults and children in the household.

FIGURE 1
Child Tax Credit, Single Parent
For one child, tax year 2021



Source: Urban-Brookings Tax Policy Center calculations.
Notes: Assumes all income comes from earnings, and child meets all tests to be a CTC-qualifying dependent. $3,000 and $3,600 credits are fully refundable; prior law limited refunds to $1,400 out of the maximum $2,000 credit. Credit for married parents first phases out at $150,000 of income until credit reaches pre-2021 level; begins second phase out at $400,000 of income. Only citizen children qualify for the $3,000 and $3,600 credits for children under 18. Noncitizens under age 18 who meet the dependency tests of eligibility can qualify other dependent credit.

As an example of these thresholds, the graph above shows the CTC schedule for a single parent with one child.[12] Lower income parents qualify for the full benefit ($3,000 or $3,600, depending on the child's age) and these benefits phase out as income exceeds $112,500. At income levels above $250,000, the worker is no longer eligible for CTC. As an example, a middle-income

[9] For further discussion of pandemic recovery suggestions, see Chang et al. (2021).
[10] https://www.cbpp.org/research/federal-tax/the-child-tax-credit
[11] https://www.taxpolicycenter.org/briefing-book/what-child-tax-credit
[12] Ibid.

family earning $55,000 in annual income with two children under 6, their total federal CTC would be $7,200.

In July 2021, there were over 59 million qualifying children in the United States with total cost to the federal government of approximately $14.9 billion.[13] The Tax Policy Center finds that 92% of families with children will receive CTC, averaging $4,380 in 2021, however, this is relatively evenly distributed across eligible households.

More details about CTC qualifications and thresholds, particularly as they relate to the changes made in 2021, can be found at the U.S. Treasury Department website or the Internal Revenue Service website.[14] The Tax Policy Center also provides an excellent overview of the program and its history.[15]

Application to CTC in Pennsylvania

Specific to Pennsylvania, there were 2.2 million qualifying children with total federal expenditures of $554.8 million.[16] If Pennsylvania enacted a state-level CTC program at 30% of the federal program, this would provide an additional credit of $900 to $1080 (depending on child's age) per qualifying child, with a total cost of approximately $166.4 million (assuming there is not an increase in participation at the federal level when the state-level policy is enacted). To continue with the earlier example of the household earning $55,000 in annual income with two children under 5, their additional payment would be $1080 per child, creating a total CTC of $9,360. For reference, the average annual cost of childcare in Pennsylvania for one preschool-aged child is $9,773.[17]

Currently, six states have enacted Child Tax Credit programs with our neighboring state of New York among them.[18] In New York, the thresholds are somewhat complicated, but many will qualify for a state CTC of 33% of the federal CTC.

Research on CTC

Relative to EITC, there is significantly less research on the effectiveness of CTC. Goldin and Michelmore (2022) and Parolin et al. (2021b) provide a summary of the scant CTC literature. Hoynes and Rothstein (2017) state that when coupled with EITC, the federal CTC program (prior to the 2021 expansion) lifts approximately 5.2 million children out of poverty, but the benefits of CTC are more evenly spread across the income distribution because higher income

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[13] https://home.treasury.gov/news/press-releases/Treasury-and-IRS-Announce-Families-of-Nearly-60-Million-Children-Receive-%2415-Billion-Dollars-in-First-Payments-of-Expanded-and-Newly-Advanceable-Child-Tax-Credit

[14] https://home.treasury.gov/news/press-releases/Treasury-and-IRS-Announce-Families-of-Nearly-60-Million-Children-Receive-%2415-Billion-Dollars-in-First-Payments-of-Expanded-and-Newly-Advanceable-Child-Tax-Credit; https://www.irs.gov/credits-deductions/advance-child-tax-credit-payments-in-2021

[15] https://www.taxpolicycenter.org/briefing-book/what-child-tax-credit

[16] https://home.treasury.gov/news/press-releases/Treasury-and-IRS-Announce-Families-of-Nearly-60-Million-Children-Receive-%2415-Billion-Dollars-in-First-Payments-of-Expanded-and-Newly-Advanceable-Child-Tax-Credit

[17] https://www.epi.org/child-care-costs-in-the-united-states/#/PA

[18] https://www.taxcreditsforworkersandfamilies.org/state-tax-credits/

households also qualify. They note that CTC also provides incentive for labor force participation as it benefits workers with qualifying dependents across a wide range of incomes, but provides few benefits for the lowest income households. Prior to the 2021 expansion, Goldin and Michelmore (2022) find that there are significant disparities in the distribution of CTC, with the highest poverty households benefiting the least and with benefits disproportionately accruing to white, non-Hispanic, and Asian children.

Following the changes in 2021, the initial CTC payment in July 2021 kept approximately 3 million children out of poverty in that month (Parolin et al., 2021a). The 2021 coverage increase overall was particularly effective at reducing childhood poverty among children of color (Curran, 2021). Other recent research by Parolin et al. (2021b) finds that the CTC payments throughout 2021 were very effective at reducing economic hardship, largely through the reduction in food insufficiency, among low-income households with children.

As with EITC, there are additional benefits accruing to families eligible for CTC as well, including health-related and education-related benefits (Parolin et al., 2021b). More broadly, there are benefits to the local economy: CTC expansion in 2021 could increase consumer spending by $27 billion, with a related increase of state and local sales tax revenue of $1.9 billion and support over 500,000 median-wage, full-time jobs (Hammond and Orr, 2021).

Considerations regarding CTC

As a policy to encourage labor force participation, EITC is likely to be more effective than CTC, as EITC is targeted to help low-income workers and the payments are relatively larger (Hoynes and Rothstein, 2017). Another concern is that, as implemented in 2021, the CTC payments did not reach all eligible families (Parolin et al., 2021b), suggesting that the full benefits of the policy were not realized.

Child and Dependent Care Tax Credit (CDCTC)

Somewhat different than the Child Tax Credit (CTC) discussed above, the Child and Dependent Care Tax Credit (CDCTC) was enacted in 1976 and is a non-refundable tax credit that offsets some of the costs of caring for a child under 13 or other dependent who is not able to work, so long as those costs are incurred due to the parent/caregiver working (Crandall-Hollick and Boyle, 2021). Prior to 2021, parents/caregivers could claim a maximum of 35% of eligible expenses up to $3,000 with one child/dependent or $6,000 with two or more children/dependents. In 2021, as part of the American Rescue Plan, CDCTC became refundable, the percentage was increased to a maximum of 50% with thresholds of $8,000 and $16,000, respectively.[19] The income thresholds for phase-out of credit also changed in 2021. In prior years, those earning more than $15,000 started to see a reduction in their CDCTC percentage at 1% per additional $2,000 in earnings

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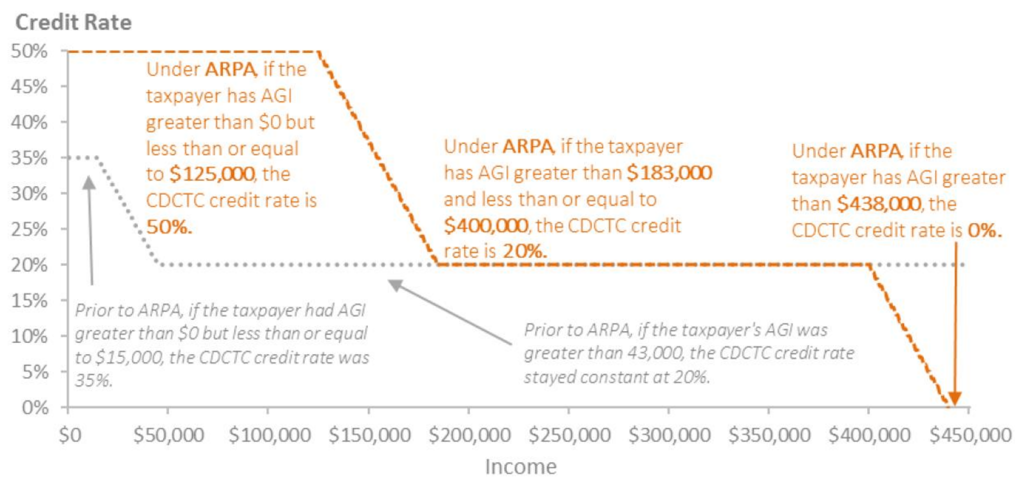
[19] https://www.irs.gov/newsroom/irs-expanded-credits-for-families-highlight-tax-changes-for-2021-many-people-who-dont-normally-file-should-file-this-year#:~:text=Child%20and%20dependent%20care%20credit%20increased%20for%202021&text=For%202021%2C%20the%20top%20credit,%243%2C000%20in%20prior%20years%2C%20or

above $15,000. In 2021, this threshold increased to $125,000 and the credit plateaus at 20% for those earning above $183,000, and finally phases out completely at $400,000. Under the 2021 policy changes, most households with qualifying children/dependents will receive a tax credit of $4,000 or $8,000.[20] The graph below illustrates these differences pre- and post-ARP expansion (Crandall-Hollick, 2021).

Child and Dependent Care Tax Credit (CDCTC) Credit Rate for 2021



Source: CRS calculations based on IRC §21 and P.L. 117-2.
Notes: Income is earned income which is assumed to equal adjusted gross income.

In 1991, over 5.9 million households claimed CDCTC benefits with a total federal cost of $2.8 billion (Gentry and Hagy, 1996). A recent Congressional report indicates that as of 2017, a total of 6.5 million children and dependents qualified for CDCTC with a total federal cost of $3.72 billion (Crandall-Hollick and Boyle, 2021).[21] This report also finds that claimants are largely in the middle of the income distribution, with relatively fewer benefits accruing to low-income families. The 2021 expansion of CDCTC is estimated to increase the federal cost to $8 billion (Crandall-Hollick, 2021).

Application to CDCTC proposal for Pennsylvania

As proposed, if Pennsylvania provided a CDCTC credit at 30% of the federal level, this would provide an additional maximum credit of $1,200 to $2,400 per household, depending on the number of children and the household income, implying total maximum federal and state credits of $5,200 to $10,400. Again, as comparison, the average annual cost of childcare in Pennsylvania for one preschool-aged child is $9,773.[22]

Currently, 24 states have enacted Child and Dependent Care Tax Credit programs. Neighboring states to Pennsylvania include Delaware, New Jersey, Maryland, New York, and Ohio.[23] Of

[20] https://www.irs.gov/newsroom/child-and-dependent-care-credit-faqs
[21] For reference, there are approximately 2.1 million children in Pennsylvania under 14 years old (Census Bureau, 2021).
[22] https://www.epi.org/child-care-costs-in-the-united-states/#/PA
[23] Details for each state can be found at https://tcwf.wpengine.com/state-tax-credits/

these, Ohio's program has the lowest thresholds, with a maximum qualifying income of $40,000 and non-refundable CDCTC of 100% for very low-income filers and 25% for those with incomes $20,000 to $40,000. Maryland has similar (though slightly different) thresholds and percentages, though Maryland's CDCTC is refundable. Delaware and New York have more generous programs, with Delaware imposing no income restriction and offering a non-refundable CDCTS of 32% of the federal credit and New York offering refundable CDCTCs of over 100% to very low-income households and 20% to households with income over $65,000.

New Jersey, which in prior years had similar thresholds and percentages to Maryland, recently increased the qualifying income level to $150,000 and made the state CDCTC refundable, estimating that an additional 800,000 households will now benefit, but these changes are in effect only for 2021 (Donyéa, 2021). This expansion was originally estimated to cost the state $17 million, but with the federal changes in CDCTC, the updated cost to New Jersey is $76 million (Symons, 2021).

Research on CDCTC

Research on CDCTC is also scarce. Several recent working papers (Pepin, 2020; Pepin, 2021) summarize this literature and analyze the effects of CDCTC on workers/households and their outcomes, and Forry and Anderson (2006) provide a detailed history of the policy. Increases in CDCTC payments have led to increases in expenditures on childcare and increases in married mother's labor supply (Pepin, 2020). Additionally, Pepin (2021) estimates that if made permanently refundable, as implemented in 2021, there are gains in eligibility and tax refunds to low-income households, particularly single parents, and Black and Hispanic households. There is also evidence that increases in CDCTC lead to increases in the price of childcare and wages of childcare workers, and when the credit is non-refundable, can have the unintended consequence of reducing affordability and access for low-income parents (Rodgers, 2018).

Considerations regarding CDCTC

One concern is that the cost of child/dependent care has increased substantially over time, but maximum amount of qualifying expenses largely has not (until the 2021 expansion). This has eroded the real value of these benefits (Crandall-Hollick, 2021). Relatedly, if implementation of CDCTC leads to large increases in childcare costs, this would reduce the net benefits of the CDCTC to working parents, which would not achieve the goal of the policy.

Another concern is that in order to claim this credit, the filer must provide a tax identification number for the care provider (Crandall-Hollick, 2021). For those who rely on informal care (e.g, in-home nanny or babysitter), as opposed to more traditional care settings (e.g., daycare center), their childcare expenses would not be eligible for credit. This may disadvantage workers who work non-traditional hours such as those working overnight shifts or with unpredictable work hours like many healthcare workers.

Finally, CDCTC interacts with Child and Dependent Care Flexible Savings Accounts (CDC FSA) that are employer-provided, and also interacts with Child Tax Credit benefits in that spending cannot be double-credited. These interactions can be complicated, leading to confusion about how much a worker/household may qualify for and therefore, may limit participation.

Conclusion

Overall, these policies enacted at the federal level, EITC in particular, have been very successful at achieving their anti-poverty goals and helping working parents. The policies proposed are similar to those already enacted in many states with bi-partisan support, including many neighboring states such as New York, New Jersey, Maryland, Delaware, and Ohio, though there are variations in qualifications and benefits across states. I have noted several considerations above that policymakers may take into account as these proposals are discussed and revised. However, in light of the current labor market situation and the childcare crisis resulting from the pandemic, policies such as these are likely to be very successful at helping working parents, particularly those with younger children. These policies may also draw some back into the labor market, with added health and human capital-related benefits to qualifying workers and their families, as well as benefits to the local economy.

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United Way of Pennsylvania

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February 15, 2022

House Democratic Policy Committee Testimony
The Cost and Benefits of Enacting a State Earned Income Tax Credit

Good morning, Chairman Bizzarro, and members of the committee. My name is Kristen Rotz, and I am the President of the United Way of Pennsylvania (UWP). The United Way of Pennsylvania is a 501(c)(3) membership organization whose mission is to champion United Way as a leader and partner in building more financially resilient families and thriving communities throughout Pennsylvania. United Way has the expertise and relationships to develop meaningful and lasting solutions to community challenges through root cause analysis. United Ways leverage donors' resources to facilitate cross-sector solutions to the problems their communities face. Through the generosity of donors, United Ways possess the ability to reduce burdens on public sector programs.

Local United Ways are also part of a national and international network which can scale solutions to achieve positive impacts across the country and around the world. In Pennsylvania, 51 local United Ways work to address community needs related to the basic building blocks for quality of life - health, income, and education. We envision an inclusive, impactful, and collaborative network of United Ways working with business, community, faith, and government leaders through the Commonwealth to advance equitable access to health, education, and financial stability for all Pennsylvanians.

As part of our work to advance financial stability, United Way of Pennsylvania is committed to lifting up ALICE through community programs and advocacy. ALICE stands for **A**sset **L**imited, **I**ncome **C**onstrained, **E**mployed. ALICE represents the 27% of Pennsylvanians that work but struggle to survive. ALICE households earn above the Federal Poverty Level but earn much less than what is needed to afford basic necessities. The Household Survival Budget estimates the actual bare-minimum costs of basic necessities (housing, child care, food, transportation, health care, and a basic smartphone plan) in Pennsylvania, adjusted for different counties and household types.

Despite the financial challenges ALICE faces, they often earn too much to qualify for public assistance. And, there is no room in ALICE's budget for an unexpected financial emergency. In March of 2020 and the subsequent months, that emergency came in the form of COVID-19. Like so many households across the Commonwealth, ALICE experienced lost wages due to unemployment or reduced working hours because of school and/or day care closures, the need to care for themselves or a sick relative, or a combination of the two. Sadly, many ALICE households are still struggling to recover.

Prior to the COVID-19 pandemic, if you combined PA households earning below the ALICE Threshold, the average income that a household needs to afford the basic necessities defined by the Household Survival

Budget for each county in Pennsylvania, with those living below the FPL, two out of five PA households faced financial hardship every day, in every county in PA. As we await the findings of the next ALICE Report©, we anticipate that the report will show an increase in the number of PA households facing financial hardship due to COVID-19. This hypothesis can be backed by the results of UWP's COVID-19 impact surveys conducted in August 2020 and March 2021. Per the UWP's second COVID-19 impact survey, entitled, "COVID-19 Impacts on Pennsylvania: The ALICE Story; One Year Later," a follow-up to our first survey, 68% of respondents with income below the ALICE threshold reported having one month or less in saving to cover basic household bills. This percentage decreased from August 2020 (77%) likely indicating that pandemic safeguards such as stimulus checks, unemployment insurance, and other forms of assistance helped Pennsylvania families financially stay afloat and save for future necessities or emergencies. With no future safeguards in place since the survey, it is likely that ALICE families, and families living over the ALICE Threshold have had to utilize savings to stay afloat as the price of goods and services continue to rise.

One way our local United Ways help struggling households is through investment or involvement in Volunteer Income Tax Assistance (VITA) sites. VITA is an Internal Revenue Service program that offers free basic tax return preparation to qualifying filers who need help preparing their income tax return. To qualify, the eligible filer must make $58,000 or less annually, have a disability, or be limited English-speaking. Currently, 20 local United Ways across the Commonwealth invest, operate, or participate in the operation of VITA sites. Through their work and investments, our local United Ways are assisting qualified ALICE households with accessing federal tax credits, such as the Earned Income Tax Credit, which provide much needed financial resources to struggling families.

Each year, the federal Earned Income Tax Credit lifts up to 6 million people out of poverty, of which about half are children. The federal Earned Income Tax Credit also reduces the degree of poverty for over 10 million more people across the United States annually. The socio-economic impacts of the tax credit have been studied by a variety of reputable sources, and one conclusion is clear: Earned Income Tax Credits are a great benefit for middle- and low-income households. According to a 2018 study conducted by the Federal Reserve Bank, Earned Income Tax Credit recipients spend the first 14 cents of every refund dollar within two weeks of receipt at retail stores and restaurants. The largest component of that spending is made at grocery stores, indicating EITC recipients do, in fact, use their refunds to "make ends meet." Other major expenditures include vehicle repairs, home repairs, and paying down credit card debt.

Whether it is financial resources to afford basic necessities, the impact on health and educational outcomes, or the effect on generational poverty, federal and state Earned Income Tax Credits are a great first step toward financial stability for many households. Therefore, United Way of Pennsylvania, and our network are advocating for the implementation of a state Earned Income Tax Credit in Pennsylvania.

Currently, 28 states and the District of Columbia offer relief to working families in the form of an Earned Income Tax Credit. Of those states, 23 offer a refundable tax credit, meaning any balance remaining, after tax liability is met, is provided in the form of a refund to the taxpayer. Studies show that refundable tax credits have a greater economic impact due to the reinvestment of the funds provided to the recipients, who typically do not save them.

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In 2021, UWP secured a grant to commission a study on the economic impact of a state Earned Income Tax Credit in Pennsylvania. In December, the Child & Family Research Partnership at the Lyndon B. John School of Public Affairs at the University of Texas at Austin completed their study and provided results, which are beyond anything UWP imagined. To further discuss those results, I am joined by United Way of Pennsylvania Public Policy Director Phil Falvo. Phil is going to provide you with an overview of “Implementing a State Earned Income Tax Credit (EITC) in Pennsylvania: A Benefit-Cost Analysis.”

Thank you for the opportunity to provide testimony on these important issues and share the perspective of the United Way of Pennsylvania, and our network of local United Ways.

Sincerely,

Kristen Rotz
President
United Way of Pennsylvania

United Way
of Pennsylvania

February 15, 2022

House Democratic Policy Committee Testimony
The Cost and Benefits of Enacting a State Earned Income Tax Credit

Good morning, Chairman Bizzarro, and members of the committee. My name is Phil Falvo, and I am the Public Policy Director at the United Way of Pennsylvania (UWP). I want to thank you for the opportunity to testify before you today about UWP's support for the enactment of an elective, refundable state Earned Income Tax Credit in Pennsylvania. For over a year, UWP has been studying this issue and the potential impact it will have on ALICE households across the Commonwealth.

On January 21, 2022, United Way of Pennsylvania released the findings of an Earned Income Tax Credit impact study titled, "Implementing a State Earned Income Tax Credit (EITC) in Pennsylvania: A Benefit-Cost Analysis," which was conducted by the Child & Family Research Partnership at the Lyndon B. John School of Public Affairs at the University of Texas at Austin. The analysis concludes that the benefits of implementing a state Earned Income Tax Credit far outweigh the costs, with every dollar invested generating $4 in economic impact and $3 in human services cost savings. Not only do households see a benefit, but local businesses and the Commonwealth will see a "trickle up" from the economic effect of the Earned Income Tax Credit.

As part of their analysis, the researchers at the Child & Family Research Partnership examined the Commonwealth's current special poverty provisions and the Tax Forgiveness Program, referred to as SP, under the Pennsylvania Department of Revenue. Because of its success in helping the lowest income households in Pennsylvania, UWP proposes to continue SP. The researchers determined the most cost-effective solution would be an elective EITC where an eligible recipient would choose between the SP and the state Earned Income Tax Credit. And, combining the two programs and making the state EITC elective would reach more families while also increasing the total value of benefits available. Depending on the value of the credit, between 715,000 and nearly 874,000 Pennsylvania households will claim a mean benefit in the ballpark of $197 and $594.

The report also reviews the effect a state Earned Income Tax Credit will have on communities in Pennsylvania who are disproportionately impacted by low income, high tax burdens, and high cost of living relative to household resources. With a 10% state EITC, 8% of White families would claim the EITC (representing 434,697 households), 17% of Black families (134,325 households), 22% of Hispanic families (101,662 households), and 13% of families reporting other race and ethnicity categories (44,968 households) would claim the credit. With a 25% state EITC, the share of each group that claims the EITC increases, because more families with dual eligibility (SP and state EITC) are likely to switch from the SP to the state EITC because the state EITC value will be presumably larger than their SP benefit.

In addition to individual impact, the report also reviews the regional impact of enactment, take-up rates and average benefits, of 10% and 25% state Earned Income Tax Credits. While the benefit is lowest at a 10% state EITC in the Norther Tier at $177, it is the lowest in the in the Northwest at $574 at a 25% state EITC. Ironically, the Lehigh Valley has the highest benefit at both the 10% and 25% state EITC, $209 and $636, respectively.

Based on United Way of Pennsylvania's prior inquiry into Earned Income Tax Credits, the team at the Child & Family Research Partnership looked at the cost of implementation of an elective, refundable state Earned Income Tax Credit at 10% and 25% of the federal credit. The projected cost for a 10% state Earned Income Tax Credit was determined to be approximately $80.5 million, including about a 1% administrative cost. For a 25% earned income tax credit, the cost rises to about $366 million.

Previous studies indicate that Earned Income Tax Credits more than pay for themselves. As the Child & Family Research Partnership indicates in their findings, a 10% state Earned Income Tax Credit in Pennsylvania, based on take up rates provided in the study, will result in about $80 million in increased Personal Income Tax revenue, $116 million in sales, payroll, and unemployment insurance taxes, and a reduction of about $190 million in public assistance spending for a grand total of $386 million in fiscal benefit. It is estimated that a 25% state Earned Income Tax Credit will generate Personal Income Tax, sales, payroll, and unemployment insurance taxes and a reduction in public assistance spend of approximately $200 million, $291 million, and $475 million, respectively. The total economic benefits for a 25% state Earned Income Tax Credit are an estimated $966 million.

In addition to fiscal benefits, the state Earned Income Tax Credit will also result in Human Services impacts and cost avoidances. The researchers analyzed the impact of the credit on child poverty, low birthweight incidence and hospital costs, need for special education, infant mortality, foster care entry, educational attainment, child health coverage, crime and public safety, and adult suicide prevention. The research team concluded that a low-end estimate of human services cost avoidance for a 10% state Earned Income Tax Cred would be approximately $176 million, and a high-end estimate would be a little over $1.8 billion. For a 25% state Earned Income Tax Credit, a low-end estimate of human services cost avoidance would be close to $214 million, and a high-end estimate would be $2.75 billion. When considering the total fiscal benefits and Human Services cost avoidance, the total project benefits would be around $562 million and $1.18 billion for a 10% and 25% state Earned Income Tax Credit, respectively.

The results of the impact study are clear, there are only winners when the Commonwealth of Pennsylvania invests in a state Earned Income Tax Credit. Considering all of our neighbors, except West Virginia, offer a state EITC to working families, Pennsylvania is a stark disadvantage when it comes to competing for younger, working households. With a state EITC, we can lift families out of poverty, while providing a path to financial stability, generating revenue, and possibly reducing tax burdens for future generations.

For more information on ALICE, please visit https://www.uwp.org/alice/about-alice/ and https://www.unitedforalice.org/pennsylvania. To review "Implementing a State Earned Income Tax Credit (EITC) in Pennsylvania: A Benefit-Cost Analysis," and other UWP Earned Income Tax Credit materials, please visit https://www.uwp.org/advocacy/eitc-study/.

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Thank you for the opportunity to provide testimony on these important issues and share the perspective of the United Way of Pennsylvania, and our network of local United Ways. I happy to answer any questions you may have about the information provided here today.

Sincerely,

Philip Falvo
Public Policy Director
United Way of Pennsylvania

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