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FIRST IN FLIGHT FROM THE EITC:

Low-Income Working Families Bid Farewell to North Carolina's Earned Income Tax Credit

BY TAZRA MITCHELL, POLICY ANALYST

2014 Marks the Loss of a Modest but Vital Support

Unless lawmakers reverse course, close to one million working families in North Carolina will claim the state Earned Income Tax Credit (EITC) for the last time this tax season, bringing pain to individual families and local economies. One year ago, North Carolina lawmakers put an end to the tax credit and subsequently pursued deep tax cuts that primarily benefit the wealthy and profitable businesses.¹ The state EITC goes to families that work but earn low wages, and helps them keep more of what they earn so that they can stay in the workforce, support their children, and avoid poverty and public assistance.

The North Carolina EITC was a vital facet of the state's tax system, building off of the federal tax credit—one of the nation's most powerful anti-poverty tools for children. Combined with the income tax cuts, the loss of the state EITC is particularly backwards because the state's tax system already asked more from low- and middle-income families than it did from those earning the most.² The resulting tax shift is neither true tax reform nor good for North Carolina's economy.

It's not too late to reverse course, however. State lawmakers can reinstate this proven policy tool during the Short Session of the legislative cycle that begins in May. If they do so, there would be no interruption to the ability of hardworking families to claim this modest but critical support during the next tax season.

State EITC Is an Essential Tool amidst Hard Times

Lawmakers established the state EITC in 2007, in the middle of two economic downturns that occurred during the 2000s. That decade represented a lost decade for families in North Carolina who faced substantial job loss, spikes in poverty, a boom in low-wage work, and prolonged deterioration in household income.³ Several years later, working families continue to face high levels of economic hardship. The state EITC plays a critical role by providing a tax reduction to low-income workers, allowing them to keep more of what they earn.

The state EITC provides a modest boost to the wages of low- and moderate-income workers.⁴ Preliminary estimates show that nearly 907,000 North Carolinians

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claimed the state EITC for tax year 2012, benefiting nearly 1.2 million children.⁵ It encourages and supports workers, and is only available to people who work and earn income from wages, salaries, or self-employment.⁶

The state EITC is a refundable credit, which means that a taxpayer can reduce their income tax liability to zero and receive a refund based on the additional value of the credit. This refund helps to offset the disproportionate share of income that low-wage workers pay in total state and local taxes—not just income taxes—compared to their wealthy counterparts. The average credit was \$119 for tax year 2012.

Value of State EITC Varied during Its Short Life

Within a six-year period, lawmakers established, strengthened, reduced, and eliminated the North Carolina EITC. In 2007, lawmakers set the original value of the North Carolina at 3.5 percent of the federal Earned Income Tax Credit. During the Great Recession, lawmakers boosted the credit to 5 percent of the federal credit to help stabilize struggling families and ease hardship. Last year, lawmakers reduced the value to 4.5 percent of federal credit for tax year 2013 and allowed it to expire thereafter. Whereas other states are maintaining and expanding their EITCs, North Carolina is the only state in the nation with a state EITC to eliminate this proven tax credit in nearly 30 years.⁷

The EITC is a Proven Anti-poverty Tool and Has Lasting, Positive Effects on Children

The EITC is widely recognized as one of the most effective anti-poverty tools nationwide, especially for children. The federal EITC lifted approximately 298,000 North Carolinians—half of whom were children—above the federal poverty line between 2010 and 2012.⁸ Similar data is not available on the state EITC, but, like the federal credit, the state credit helps low-wage workers pay for basic needs such as shelter, food, and utilities, as well as work-related costs such as transportation and child care. The state EITC builds upon the success of the federal credit and its loss could push more families into poverty at a time when North Carolina has the 10th highest poverty and child poverty rates in the nation.⁹

The EITC is mostly used as a temporary support. Three out of five recipients claim this tax credit for short periods—only one or two years at a time.¹⁰ As such, this tax credit is an effective way to help families stay on their feet by offsetting short-term struggles resulting from job loss, reduced hours, or reduced pay. The benefits of the EITC are long-lasting and positive too: low-income children in families that get additional income through tax policies like the EITC perform better in school, are more likely to attend college, and earn more as adults on average.¹¹

Loss of State EITC Is a Losing Strategy for North Carolina and Its 100 Counties

Working families in each of the state's 100 counties benefit from the state EITC, which was valued at nearly \$107.7 million in tax year 2012 (see the Appendix). This cost is small: \$107.7 million is less than 10 percent of the income tax cuts provided to the wealthy and big businesses under the fully-implemented tax plan.¹² This tax credit helps small businesses that pay low wages, particularly in the eastern parts of the state that have the highest concentrations of EITC recipients.

The state EITC is a small investment that helps local economies and ensures that hard-working North Carolinians are able to meet basic needs and avoid raising their children in poverty, despite low wages. Today, with low-income working families battered by unparalleled economic challenges, the state EITC plays a particularly vital role. Because now is precisely the wrong time to further shift the tax load onto North Carolina's lowest-paid workers—especially those with children to support—lawmakers should quickly reinstate the state EITC during the upcoming Short Session.

- 1 Johnson, Cedric. "Final Tax Plan Falls Short of True Tax Reform." NC Budget and Tax Center. 2013. Available here: <http://www.ncjustice.org/?q=budget-and-tax/btc-reports-final-tax-plan-falls-far-short-true-tax-reform>
- 2 Institute on Taxation and Economic Policy. "Who Pays? A Distributional Analysis of the Tax Systems in All 50 States." 2013.
- 3 Mitchell, Tazra. "The Lost Decade: Low- and Moderate-Income Families Lose Ground as Unemployment and Poverty Rise in NC." NC Budget and Tax Center. 2011. Available here: <http://www.ncjustice.org/?q=btc-brief-lost-decade-low%E2%80%90and-moderate%E2%80%90income-families-lose-ground-unemployment-and-poverty-rise-nc>
- 4 To qualify for the EITC in 2012, workers must have earned less than \$13,980 to \$45,060, depending on the worker's marital status and number of dependent children.
- 5 Special data request to the North Carolina Department of Revenue. February 2014.
- 6 Nada Eissa and Hilary Hoynes. "Behavioral Responses to Taxes: Lessons from the EITC and Labor Supply." Tax Policy and the Economy. October 2006.
- 7 Wisconsin enacted a nonrefundable EITC in 1983, only soon to repeal the credit in 1985. A few years later, in 1989, Wisconsin reinstated the EITC, but this time as a refundable credit.
- 8 Brookings Institution. "State Estimates of People and Children Lifted out of Poverty by EITC and CTC per Year, 2010-2012." 2014. Available here: http://www.brookings.edu/~media/Research/Files/Blogs/2014/02/11%20eitc/EITC_CTC%20State%20Table.pdf
- 9 Author's analysis of the United States Bureau of the Census' 2012 American Community Survey.
- 10 Tim Dowd and John B. Horowitz. "Income Mobility and the Earned Income Tax Credit: Short-Term Safety Net or Long-Term Income Support." Public Finance Review. September 2011.
- 11 Marr, Chuck et al. "Earned Income Tax Credit Promotes Work, Encourages Children's Success at School, Research Finds: For Children, Research Indicates that Work, Income, and Health Benefits Extend Into Adulthood." Center on Budget and Policy Priorities. 2013. Available here: <http://www.cbpp.org/cms/?fa=view&id=3793>
- 12 Under the new tax plan, the cuts in the personal income tax and corporate income tax—which primarily benefit the wealthy and big businesses—will cost approximately \$1.4 billion annually when the tax plan is fully implemented in the 2018 fiscal year. The \$1.4 billion estimate is based on the Fiscal Note prepared by the North Carolina General Assembly's Fiscal Research Division. The cost of the EITC as a share of the total income tax cuts could shrink even more if the corporate income tax rate is further reduced, which is set to happen if specified revenue targets are met beginning in the 2016 fiscal year.

County	Total EITC Reported		
	Number of Returns*	Number of Qualifying Children	Total Credit Value (\$)
Alamance	14,626	19,289	1,759,085
Alexander	3,212	4,276	366,821
Alleghany	985	1,210	106,851
Anson	3,205	4,386	427,649
Ashe	2,434	2,811	252,768
Avery	1,429	1,565	146,352
Beaufort	5,126	6,850	660,738
Bertie	2,679	3,670	351,311
Bladen	3,760	5,278	488,386
Brunswick	8,431	10,563	968,295
Buncombe	20,520	23,541	2,127,185
Burke	7,955	10,304	908,861
Cabarrus	14,428	19,769	1,723,452
Caldwell	8,102	10,460	958,578
Camden	606	785	65,452
Carteret	5,303	6,112	564,365
Caswell	2,319	2,924	268,935
Catawba	14,977	19,697	1,743,502
Chatham	3,959	5,212	450,090
Cherokee	2,546	3,284	300,905
Chowan	1,609	2,164	206,970
Clay	951	1,180	107,152
Cleveland	10,345	14,192	1,287,496
Columbus	6,555	9,098	857,672
Craven	8,568	11,496	1,031,688
Cumberland	31,752	43,961	4,034,901
Currituck	1,582	1,967	173,514
Dare	2,722	3,133	275,425
Davidson	15,071	19,724	1,764,884
Davie	2,999	3,996	340,998
Duplin	6,147	8,807	812,892
Durham	23,943	31,304	2,903,174
Edgecombe	8,276	11,625	1,156,384
Forsyth	30,913	40,352	3,739,634
Franklin	5,194	7,261	636,921
Gaston	19,741	26,118	2,371,158
Gates	906	1,227	108,167
Graham	846	1,137	101,232
Granville	4,843	6,625	572,572
Greene	1,996	2,833	265,093
Guilford	47,545	61,358	5,760,018
Halifax	7,533	10,306	995,967
Harnett	10,161	14,372	1,254,612
Haywood	5,084	6,025	561,490
Henderson	7,868	9,870	872,272
Hertford	2,708	3,720	360,408
Hoke	4,963	7,186	663,836
Hyde	507	659	61,796
Iredell	13,013	17,066	1,479,914
Jackson	2,838	3,294	295,501
Johnston	14,148	20,131	1,728,960

County	Total EITC Reported		
	Number of Returns*	Number of Qualifying Children	Total Credit Value (\$)
Jones	955	1,257	113,306
Lee	5,935	8,372	741,147
Lenoir	7,410	10,194	960,924
Lincoln	5,726	7,524	659,769
Macon	2,920	3,506	321,250
Madison	1,908	2,292	211,249
Martin	2,532	3,353	318,761
McDowell	4,239	5,600	493,732
Mecklenburg	85,331	114,514	10,758,579
Mitchell	1,281	1,600	141,575
Montgomery	2,703	3,702	349,818
Moore	6,857	8,863	812,486
Nash	11,234	15,411	1,449,234
New Hanover	15,121	17,204	1,571,993
Northampton	2,377	3,274	312,271
Onslow	12,901	17,414	1,498,404
Orange	6,912	7,769	685,705
Pamlico	1,132	1,408	132,792
Pasquotank	3,882	5,126	480,870
Pender	4,458	5,975	525,417
Perquimans	1,151	1,542	147,718
Person	3,762	4,805	435,336
Pitt	16,755	22,527	2,179,889
Polk	1,444	1,805	162,370
Randolph	13,123	17,676	1,568,385
Richmond	6,065	8,537	841,317
Robeson	18,368	25,955	2,548,008
Rockingham	8,907	11,454	1,032,920
Rowan	13,307	18,148	1,635,729
Rutherford	6,391	8,515	762,577
Sampson	7,035	9,995	892,979
Scotland	5,046	7,248	699,882
Stanly	5,352	7,008	610,847
Stokes	3,721	4,858	421,082
Surry	6,512	8,550	765,613
Swain	1,889	2,422	205,240
Transylvania	2,472	2,995	274,545
Tyrrell	506	673	63,327
Union	13,517	19,506	1,651,352
Vance	6,088	8,404	787,124
Wake	59,711	77,899	6,882,415
Warren	2,167	2,973	273,968
Washington	1,620	2,174	204,305
Watauga	2,874	2,873	259,358
Wayne	12,071	16,837	1,524,017
Wilkes	6,815	8,786	798,285
Wilson	10,195	14,082	1,341,101
Yadkin	3,263	4,216	375,622
Yancey	1,555	1,919	167,928
TOTAL	906,916	1,197,969	107,660,805

SOURCE: North Carolina Department of Revenue. Preliminary Run of 2012 Individual Income Tax Extract. February 2014. *Total includes tax filing not assigned to a county.