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## A Tax Cut That Works for Working Families: A West Virginia Earned Income Tax Credit

*Sean O'Leary*

Too many working families in West Virginia are paid low wages and have trouble making ends meet, with basic living expenses stretching family budgets beyond their limits. With tax overhaul a main topic in front of the legislature, a bottom-up tax cut like a state Earned Income Tax Credit that would help people who work hard for low pay should be central to the discussion.

The federal EITC is a common-sense tax break that helps working families. It is available only to people who work, and helps them keep working despite low wages -- which benefits families and local economies. It grows in size with each additional dollar earned, up to a modest income level, to reward and encourage more work. And because it reduces hardship, it has lasting benefits for children in struggling families, putting them on a path to a better future. States can build on the successes of the federal credit by adopting their own version of it, as 26 have already done.

A pro-work, West Virginia EITC modeled after the federal credit would allow low-paid families to keep more of what they earn, reduce the substantial state and local taxes they pay, and give a boost to local businesses. Relative to other kinds of tax cuts, it's a targeted and modest investment that can make a big difference for thousands of working West Virginia households in every corner of our state.

### Key Findings

- **EITCs provide a bottom-up tax cut for working families.** The federal EITC benefited 157,000 low and moderate income tax filers in West Virginia in 2014, with an average benefit of \$2,214. Working West Virginians across the state, in fields as diverse as health care, retail, and construction, stand to gain from creating a state EITC.
- **State EITCs make upside down state tax systems fairer.** While the federal EITC offsets federal income and payroll taxes, low- and moderate-income families in West Virginia pay more of their income and state and local taxes than wealthier families. A state EITC would help those low-income families who are paying more in state and local taxes.
- **State EITCs are popular and have broad support.** 26 states have enacted state versions of the EITC, making their tax systems fairer, and building on the federal credit's success at reducing poverty and encouraging work.
- **A state EITC would boost small businesses, local economies, and West Virginia's future workforce.** Set at 15% of the federal credit, a West Virginia EITC would benefit 141,000 low- and moderate-income households, including 161,000 children, across all 55 counties, pumping millions into West Virginia's communities and giving customers more disposable income to spend in their community. It would also strengthen the foundation for young people who make up West Virginia's future workforce, as research shows that children in families who receive the EITC are likelier to excel in school, graduate high school, attend college, and earn more as adults.

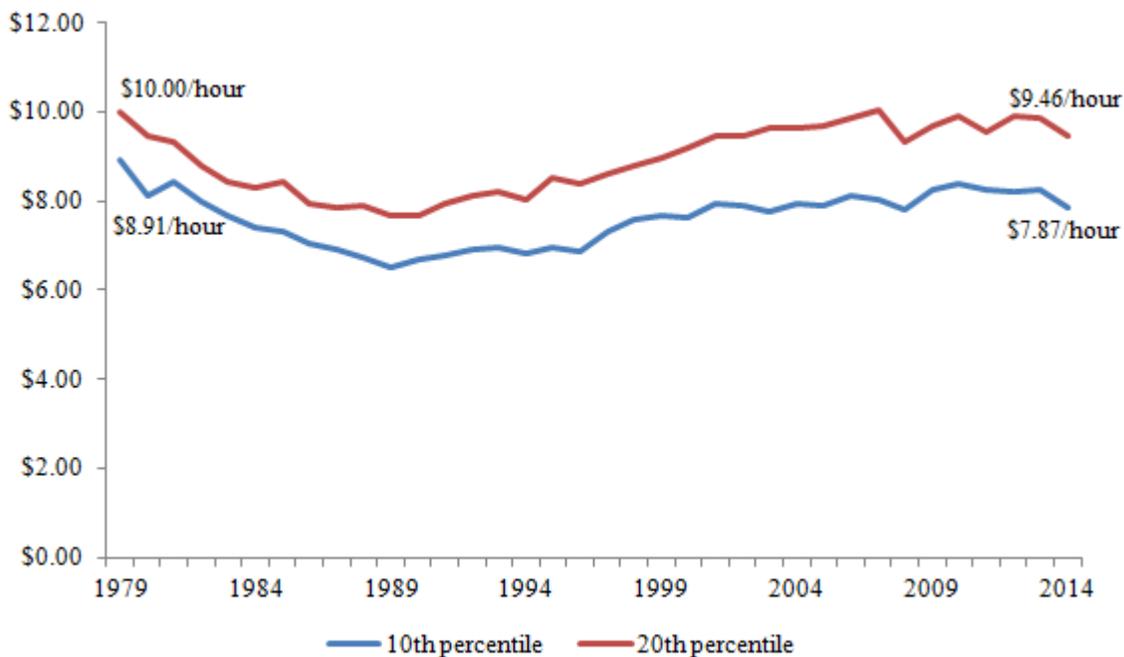
## Working Families Struggle with Low Wages

For many West Virginians, it is impossible to meet basic needs, no matter how hard they work because wages have not kept up with the cost of living. Wages for West Virginians earning the least have declined by five percent over the last 35 years, after adjusting for inflation, leaving low-income workers in West Virginia earning less today than they did in 1979, when it comes to the purchasing power of what they make. That's a major reason why West Virginia's poverty rate remains chronically high, topping 18 percent in 2014.<sup>i</sup> At the current minimum wage of \$8.00 per hour, a single mom working full time and providing for two children would have income \$2,433 below the official poverty line of about \$19,073.

### Figure 1

*Many West Virginians Are Paid Less Today than in 1979*

*(Real Hourly Wages, 10<sup>th</sup> and 20<sup>th</sup> Percentile, West Virginia, 1979-2014, 2014 dollars)*



Source: Economic Policy Institute analysis of Current Population Survey data.

In January 2016, West Virginia's minimum wage is scheduled to increase to \$8.75 per hour, raising the annual incomes for full-time minimum wage earners to \$18,200. Even with this increase, working full-time for the minimum wage won't lift a family of three out of poverty.

Beyond poverty, more than half of West Virginians are living on substandard incomes. For example, according to the Economic Policy Institute's Family Budget Calculator, a family of three (two parents, one child) living in Charleston needs \$54,248 per year to secure an adequate but modest living standard,<sup>ii</sup> well above the Charleston metro area's median household income of \$42,761.<sup>iii</sup>

## The EITC Encourages Work and Has Lasting Benefits for Children

The EITC provides a strong incentive for people to get jobs and keep them,<sup>iv</sup> despite low wages. This is especially true of single women with young children and low education.<sup>v</sup> Expansions of the EITC in the mid-1990s are credited with helping move half a million families from cash welfare to work.<sup>vi</sup> With the lowest labor force participation rate in the country, West Virginia could help workers stay on the job by creating a state EITC. Often

families use the EITC to help pay for the very things that allow them to work, like reliable transportation or child care.

The federal EITC is a credit against federal income taxes that boosts the wages of low- and moderate- income workers, and in doing so, encourages people to keep working, decreases their need for public benefits, and helps them move toward the middle class. The credit is refundable, meaning that working families get to keep the full value of the credit they earned even if it exceeds the income taxes they owe. In doing so it helps offset the other taxes people pay even if they owe little or no income tax – likes sales, gas, and property taxes.

The amount of the EITC depends on a family’s income, marriage status, and number of children. The credit’s value grows to a certain threshold, with the largest credit going to parents making about \$10,000 to \$23,000 a year, who can receive a credit of up to \$6,242. The value of the credit gradually phases out as workers earn more, and is fully phased out at incomes between \$39,000 and \$53,000, depending on marriage status and number of children.<sup>vii</sup> The unique structure of the EITC provides the most help to families as they escape poverty, but still provides value as families improve their financial security.

In West Virginia, approximately 157,000 tax filers, 21 percent of all tax filers in the state, received \$347 million in federal EITC benefits in 2013, with an average credit amount of \$2,214. The vast majority of EITC benefits in West Virginia went to workers with children: 70 percent of tax filers who claimed the EITC in West Virginia had at least one child, while 93 percent of the \$347 million in benefits went to tax filers with children.<sup>viii</sup> Overall, more than 412,000 West Virginians live in an EITC-eligible household, including more than 174,000 children.<sup>ix</sup>

The income boost provided by the EITC, along with the federal Child Tax Credit, reduces the struggles that thousands of West Virginia families face. Together, the credits lifted 38,000 West Virginians, including 18,000 children, out of poverty each year, on average, from 2011 to 2013.<sup>x</sup> This is a very big deal for children. Children in struggling families receiving the EITC experience several benefits that result from them having their basic needs met. And this, in turn, strengthens West Virginia’s future economy. For example, children in families who receive the EITC have been found to have higher elementary school test scores,<sup>xi</sup> higher rates of high school graduation and college attendance,<sup>xii</sup> and higher earnings as adults.<sup>xiii</sup>

**LASTING IMPROVEMENTS IN THE LIVES OF CHILDREN**

The EITC lifts children out of poverty and is associated with healthier babies, improved educational outcomes, and higher rates of employment and earnings later in life.

 <p><b>HEALTHIER BABIES</b> An expanded EITC is associated with improvements in birth weight and fewer premature births.</p>	 <p><b>BETTER EDUCATIONAL OUTCOMES</b> Raising family income through refundable tax credits makes it more likely that children will attend college.</p>	 <p><b>INCREASED EARNINGS</b> Adding \$3,000 a year in EITC income to families with young children is associated with a 17 percent increase in those kids’ annual earnings as adults.</p>
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The EITC is primarily a short-term income support. Most families claim the EITC for just one or two years at a time during hard times, and often their improving financial circumstances result in families leaving EITC eligibility. Over 40 percent of EITC filers claim the credit for one year at a time, and just 19 percent claim the

credit for two consecutive years; only 2.3 percent of filers reclaim the credit after five years of not having claimed the credit.<sup>xiv</sup>

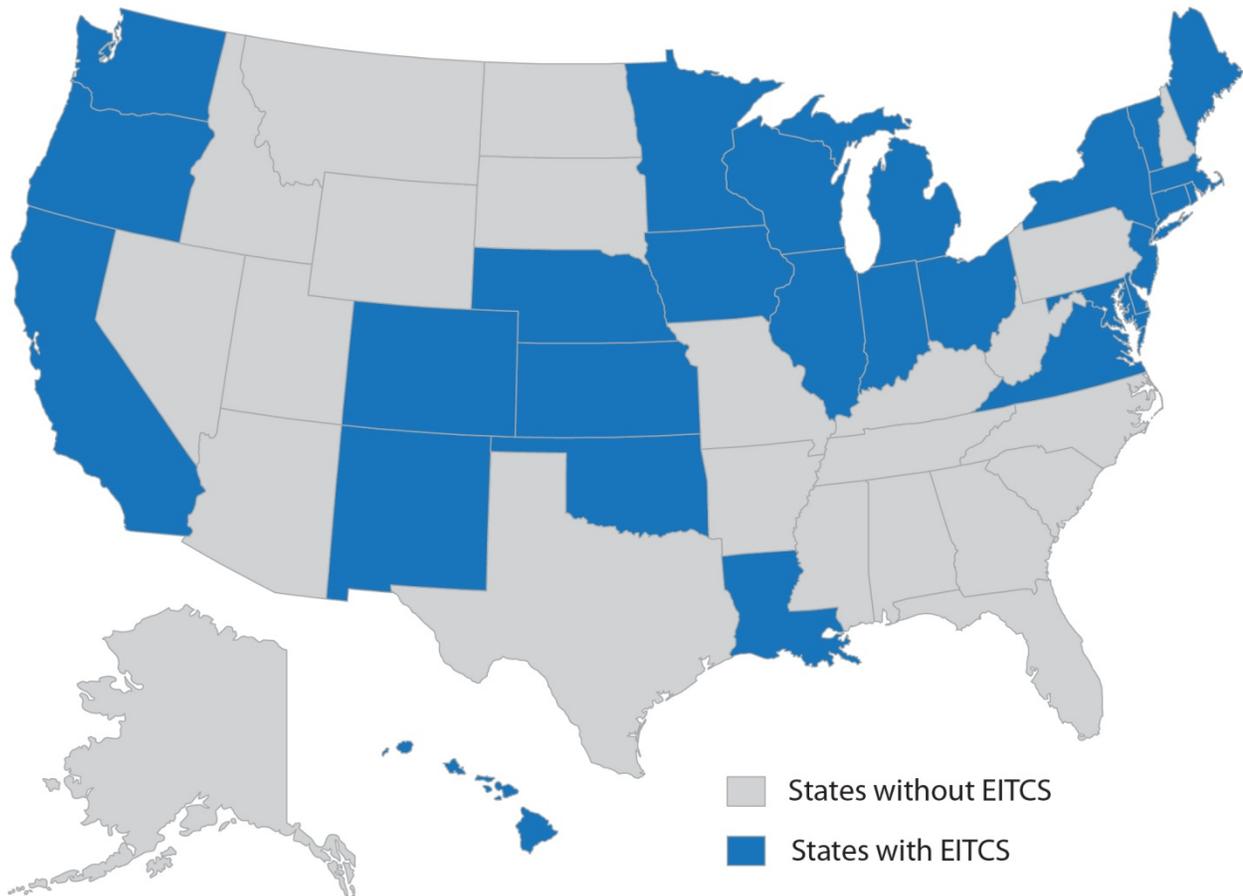
The EITC also boosts local economies, by putting more money in the pockets of those who earn low wages and who are most likely to spend their money in their community,<sup>xv</sup> creating a ripple effect throughout the economy. Various studies have shown that the federal EITC has a large economic “multiplier effect,” with every \$1 of EITC realized by local taxpayers generating between \$1.07 and \$1.67 worth of local economic activity.<sup>xvi</sup>

Recognizing the considerable value of the federal EITC, 26 states and the District of Columbia have enhanced the federal credit with their own state-level EITCs. State EITCs provide an additional boost for taxpayers who already receive the federal EITC. Only taxpayers who are eligible for the federal credit receive the state credit, and the state EITCs are typically claimed as a percentage of the federal credit’s value. State EITCs range from 3.5 percent to 40 percent of the federal credit.<sup>xvii</sup>

All but three of these states allow working families to keep the full value of the credit they earned, even if it exceeds their state income taxes. This feature allows the state credit to reduce the full range of state and local taxes households pay, especially those that eat up the biggest share of struggling families’ paychecks, like sales taxes.

### Map 1

*Twenty-Six States Already Have Their Own Earned Income Tax Credit*



Source: Center on Budget and Policy Priorities

## A West Virginia EITC Would Offer a Bottom-Up Tax Cut

A West Virginia EITC would cut taxes for those who need it most: workers in low-wage jobs. Unlike simply reducing tax rates, which disproportionately favors the wealthy, the EITC cuts taxes from the bottom up, rather than the top down. By enacting a state EITC, West Virginia would build upon the positive aspects of the federal credit, which include helping reduce poverty, improving the workforce, and increasing tax fairness.

A West Virginia EITC set at 15 percent of the federal credit would put an estimated \$46.9 million annually into the pockets of about 141,000 working households, including about 162,000 children. If a family earned a \$3,000 federal credit, it would also receive a \$450 state credit.

The working families that would benefit not only face stagnant wages. They are also paying a larger portion of their incomes toward state and local taxes than wealthier families. For example, on average, families with earnings of \$16,000 a year pay 8.7 percent of their incomes toward state and local taxes in West Virginia, while those in the top 1 percent – making on average \$675,800 a year - pay 6.5 percent (**Figure 2**).

A West Virginia EITC would also make the state’s tax system fairer. A state EITC set at 15 percent of the federal credit would lower the amount of state and local taxes paid by low income families in West Virginia to an average of 7.6 percent of their income, from 8.7 percent (**Figure 2**).

**Figure 2**

*Low- and Moderate Income Families Pay More in State and Local Taxes*  
*West Virginia state and local taxes as a share of non-elderly family income, 2015*



Source: Institute on Taxation and Economic Policy

Below are three hypothetical examples of West Virginian families who would benefit from a state EITC. These examples assume that a state EITC in West Virginia would be set at 15 percent of the federal credit.

### *Single Mother, One Child*

A single mother of one, working full-time at \$9.00 per hour, would earn \$18,720 a year before taxes. She would owe about \$489 in West Virginia income taxes for 2014.<sup>xviii</sup>

A refundable state EITC at 15 percent of the federal credit would work out to \$474,<sup>xix</sup> reducing her state income tax owed to just \$15 from \$489, nearly offsetting all of her state income tax, and enabling her to use the savings for child care or furthering her education.

### *Married Couple, Two Children*

A married couple with two children, and a combined income of \$30,000, would owe about \$780 in West Virginia state income taxes for 2014.<sup>xx</sup>

A refundable 15 percent state EITC comes out to about \$605 for them,<sup>xxi</sup> dropping the West Virginia income tax bill down to \$175. The family can use its savings for transportation, child care, and other investments necessary for staying employed and moving to the middle class.

### *Married Couple, Three Children*

A married couple with three children, and a combined income of \$40,000, would owe about \$1,125 in West Virginia state income taxes for 2014.<sup>xxii</sup>

Because this family is nearing the middle class, the EITC has begun to gradually phase out and their West Virginia EITC would equal \$289,<sup>xxiii</sup> reducing their state income tax bill to \$836.

The benefits of a West Virginia EITC would be felt across the state. In 2013, the EITC delivered \$347 million to working West Virginians all across the state. Households receiving the EITC are in nearly every community in West Virginia. As the map below shows, at least 20 percent of households filing a federal income tax return claimed the EITC in 43 of West Virginia's 55 counties in 2013. Because the families who receive the EITC spend nearly every dollar they earn on necessities, the money that helps them provide for their children will flow right back into the economy and give a boost to local businesses.

## **Paying for a State EITC**

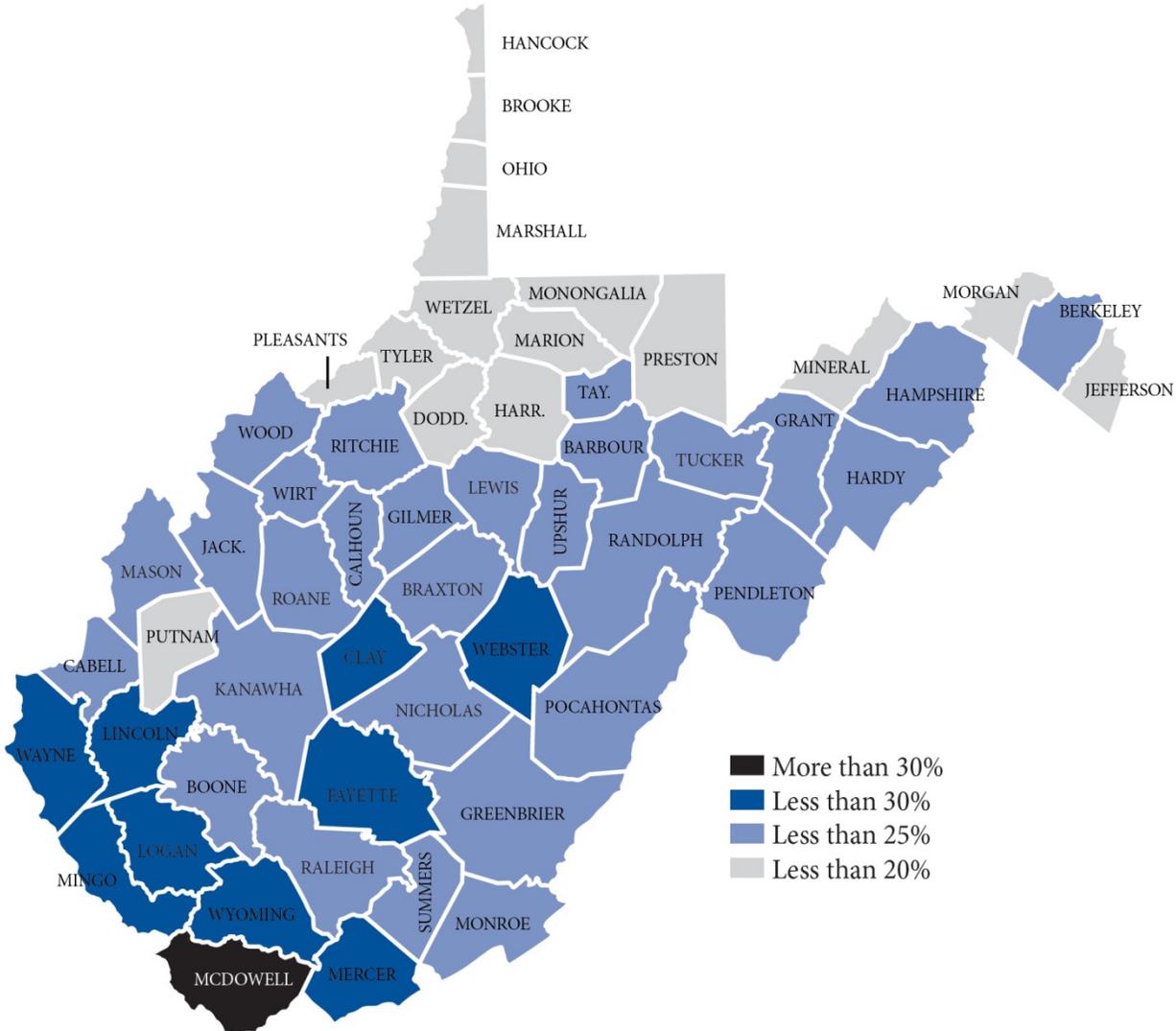
At a time when the state is facing significant revenue shortfalls, any tax shift that reduces state revenue should be approached with caution. A West Virginia EITC would carry a modest cost with a good return on investment. A West Virginia EITC set at 15 percent of the federal credit would cost about \$46.9 million, all of which would be put in the pockets of 141,000 hardworking families in West Virginia. West Virginia has numerous options to offset this investment. For example, the Family Tax Credit (FTC) currently costs about \$19 million annually. Assuming that taxpayers would be required to choose one credit or the other, or that the EITC simply replaces the FTC, that \$19 million would offset a large portion of the EITC's costs.

Other options include raising the state's tobacco tax. At 55 cents per pack, West Virginia's cigarette tax is lower than all but six states<sup>xxiv</sup>, and the state has a very low tax on non-cigarette tobacco products.<sup>xxv</sup> Increasing the cigarette tax to \$1.55 per pack and increasing the tax on other tobacco products to 50 percent of wholesale price would provide an estimated \$137.2 million in additional revenues and put West Virginia near the national average of \$1.54 per pack -- more than enough to pay for a state EITC.<sup>xxvi</sup> In addition, under federal law, states can use Temporary Assistance for Needy Families (TANF) funding to cover the refundable share of a state EITC going to working families with children, which accounts for most of that cost.

Finally, since the IRS determines eligibility requirements for the federal EITC and calculates the family’s base credit, a state EITC could be implemented in West Virginia with minimal administrative costs.

**Map 2**

*Across the State, West Virginians Earning Low Wages Rely on the Federal Earned Income Tax Credit*



Source: WVCBP analysis of Brookings Institute data

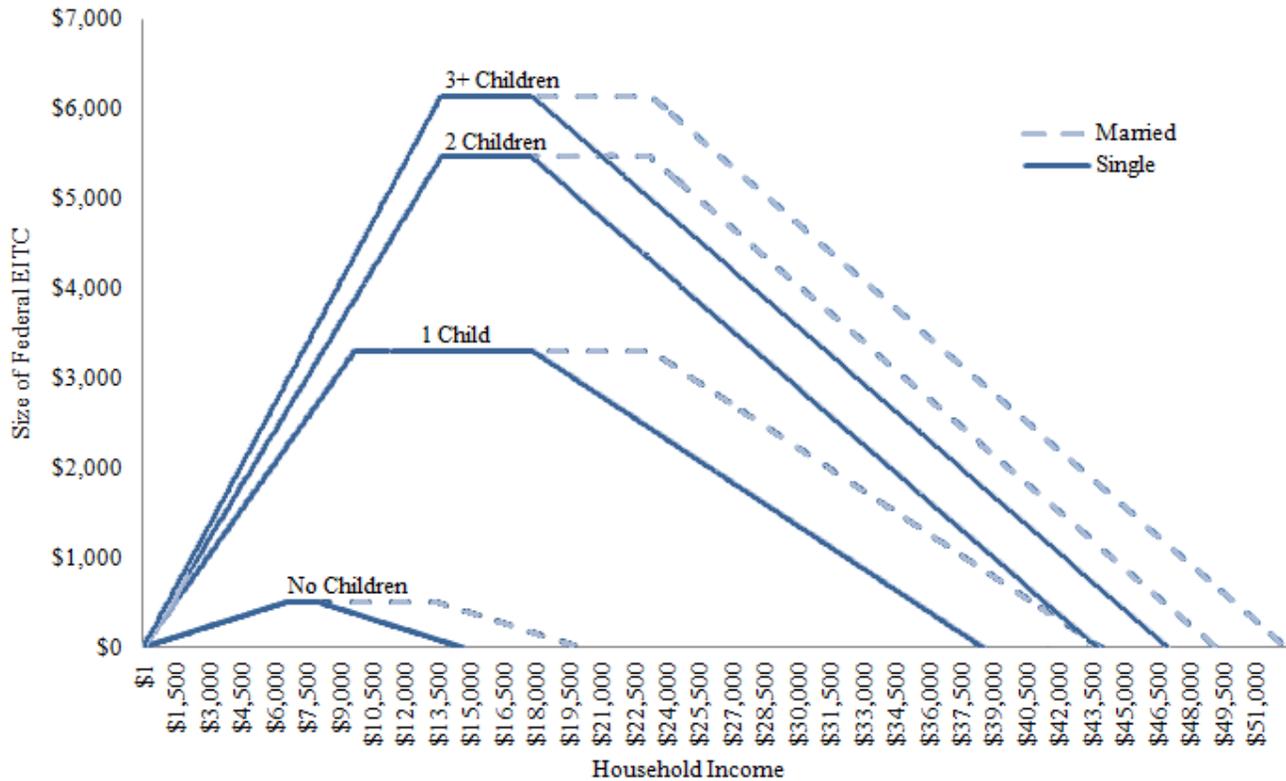
**Conclusion**

West Virginia has the opportunity to be the 27<sup>th</sup> state to build on the undeniable success of the federal Earned Income Tax Credit of encouraging work, reducing the struggles of low-paid families, and building a better future for children. A West Virginia EITC would help over 141,000 hard-working West Virginians in every part of the state make ends meet by reducing the substantial share of income they spend on state and local taxes.

As the legislature considers changes to taxes in West Virginia, a high priority should be an affordable, bottom-up tax cut that keeps people working and gives local businesses a boost. The experience from the federal credit and the 26 states with their own credit makes it clear that a state EITC in West Virginia can help build the middle class, strengthen communities, and keep West Virginians in the workforce.

## Appendix

### Federal EITC value by income, marriage status, and number of children, 2014



Source: 2014 Earned Income Tax Credit Table, Internal Revenue Service  
Federal EITC value by income, marriage status, and number of children, 2014

### West Virginia EITC Return Data by Adjusted Gross Income, 2013

Adjusted Gross Income	Number of EITC Returns
Less than \$5,000	16,082
\$5,000 to \$9,999	26,843
\$10,000 to \$14,999	31,291
\$15,000 to \$19,999	19,108
\$20,000 to \$24,999	13,720
\$25,000 to \$29,999	10,922
\$30,000 to \$34,999	9,011
\$35,000 to \$39,999	6,793
\$40,000 to \$49,999	6,022

Source: Brookings Institute, EITC Interactive Data

### West Virginia EITC Return Data, 2013

Total Number of Tax Returns	746,233
Total Returns Claiming EITC	156,866
Total Value of EITC Benefit	\$347,260,928
Average EITC Benefit	\$2,214

Source: Brookings Institute, EITC Interactive Data

### Characteristics of EITC Eligible Tax Filers in West Virginia, 2013

Estimated Total Tax Filers	724,178
Estimated EITC Eligible Tax Filers	161,872
Total Population EITC Eligible	412,849
Total Population EITC Eligible - Children	174,781
Median adjusted gross income	\$12,594
<b>Filing Status</b>	<b>Share of EITC Eligible Filers</b>
Married Filed Jointly	28.1%
Head of Household	44.7%
Single	27.2%
<b>Race</b>	<b>Share of EITC Eligible Filers</b>
White	90.2%
Black	5.8%
Other	3.9%
<b>Educational Attainment</b>	<b>Share of EITC Eligible Filers</b>
High school or less	58.5%
Some college or associate's degree	32.2%
Bachelor's degree or higher	9.3%
<b>Industry</b>	<b>Share of EITC Eligible Filers</b>
Health care	14.1%
Retail trade	13.3%
Accommodation and food service	12.5%
Construction	7.9%
Other services	7.5%
<b>Occupation</b>	<b>Share of EITC Eligible Filers</b>
Office and administrative	11.3%
Sales	10.8%
Construction, extraction	9.2%
Transportation and material moving	8.9%
Building and grounds cleaning and maintenance	8.3%

Source: The Brookings Institute, Characteristics of the EITC-Eligible Population

### West Virginia EITC Return Data by Qualifying Children, 2013

Number of Qualifying Children	Number of EITC Returns	Amount of EITC Received
0 qualifying children	39,142	\$10,836,044
1 qualifying child	56,553	\$126,839,466
2 qualifying children	37,012	\$129,333,121
3 or more qualifying children	16,803	\$66,044,075

Source: Brookings Institute, EITC Interactive Data

## Endnotes

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- <sup>i</sup> 2014 American Community Survey
- <sup>ii</sup> Family Budget Calculator, Economic Policy Institute, <http://www.epi.org/resources/budget/>
- <sup>iii</sup> 2014 American Community Survey
- <sup>iv</sup> V. Joseph Hotz and John Karl Scholz, "The Earned Income Credit," 173-176, in Robert A. Moffitt, ed., in Means Tested Transfer Programs in the United States, Chicago: University of Chicago Press, January 2003
- <sup>v</sup> Nada Eissa and Hilary Hoyes, "Behavioral Responses to Taxes: Lessons from the EITC and Labor Supply," National Bureau of Economic Research, Working Paper 11729, November 2005, pp.14.
- <sup>vi</sup> "The Earned Income Tax Credit and Transfer Programs: A Study of Labor Market and Program participation," Tax Policy and the Economy, Vol. 9, MIT Press, 1995.
- <sup>vii</sup> 2014 Earned Income Tax Credit Table, Internal Revenue Service, Publication 596 - Additional Material
- <sup>viii</sup> Earned Income Tax Credit (EITC) Interactive Resources, Brookings Institute, April 15, 2014. Retrieved from <http://www.brookings.edu/research/interactives/eitc>
- <sup>ix</sup> "Characteristics of the EITC-Eligible Population," Brookings Institution. 2013
- <sup>x</sup> "West Virginia Fact Sheet: Tax Credits Promote Work and Fight Poverty," Center on Budget and Policy Priorities. <http://apps.cbpp.org/3-5-14tax/?state=WV>
- <sup>xi</sup> "EITC and Child Tax Credit Promote Work, Reduce Poverty, and Support Children's Development, Research Finds," Center on Budget & Policy Priorities. April 3, 2015.
- <sup>xii</sup> Ibid.
- <sup>xiii</sup> "Early-Childhood Poverty and Adult Attainment, Behavior, and Health," Child Development. January/February 2010, pp. 306-325
- <sup>xiv</sup> National Community Tax Coalition, (2012).
- <sup>xv</sup> Howard Gleckman, "Tax cuts for the rich don't boost the economy. Tax cuts for the poor might." The Christian Science Monitor, April 22, 2015.
- <sup>xvi</sup> National Community Tax Coalition, "The Earned Income Tax Credit, Good for Families, Communities and Economy," (January 2012).
- <sup>xvii</sup> "States With EITCs," Tax Credits for Working Families. <http://www.taxcreditsforworkingfamilies.org/earned-income-tax-credit/states-with-eitcs/>
- <sup>xviii</sup> 2014 Personal Income Tax Form, WV Tax Department
- <sup>xix</sup> 2014 Earned Income Tax Credit Table, Internal Revenue Service, Publication 596 - Additional Material
- <sup>xx</sup> 2014 Personal Income Tax Form, WV Tax Department
- <sup>xxi</sup> 2014 Earned Income Tax Credit Table, Internal Revenue Service, Publication 596 - Additional Material
- <sup>xxii</sup> 2014 Personal Income Tax Form, WV Tax Department
- <sup>xxiii</sup> 2014 Earned Income Tax Credit Table, Internal Revenue Service, Publication 596 - Additional Material
- <sup>xxiv</sup> See Federal Tax Administrators, State Excise Rates on Cigarettes (January 1, 2015). Retrieved from [www.taxadmin.org/fta/rate/cigarette.pdf](http://www.taxadmin.org/fta/rate/cigarette.pdf).
- <sup>xxv</sup> States tax other tobacco tax products using different methods. According to Tobacco Free Kids, they calculate the average rate among states to be 45.4 percent of wholesale price. See Campaign for Tobacco-Free Kids, State Excise Tax Rates for Non-Cigarette Tobacco Products. Retrieved from [www.tobaccofreekids.org/research/factsheets/pdf/0169.pdf](http://www.tobaccofreekids.org/research/factsheets/pdf/0169.pdf).
- <sup>xxvi</sup> See fiscal note on Senate Bill 534 in 2014 Legislative Session. Retrieved from [http://www.legis.state.wv.us/FiscalNotes/FN%282%29/fnsubmit\\_recordview1.cfm?RecordID=20057555](http://www.legis.state.wv.us/FiscalNotes/FN%282%29/fnsubmit_recordview1.cfm?RecordID=20057555).