

WEALTH BUILDING

Earned Income Tax Credit

Working Hands Getting a Hand Up



Who should use this information?

The Earned Income Tax Credit is a valuable tool to help working, low-income people keep more of their earnings. This document is intended to benefit any organization or institution working to help or interested in helping families become more financially secure. They can be:

- Nonprofits helping low-income families lift themselves out of poverty;
- Banks encouraging people to start savings accounts;
- Faith-based organizations providing additional services to their congregants and communities;
- Public schools or after-school programs providing financial education, enabling students to help their families maximize their annual incomes; and
- Legislative aides or legislators seeking to improve policy, building upon the availability of EITC.

Building Wealth in the Mid South



When low-wealth families are provided the tools to save and grow their money, the generational cycle of poverty can be broken.

The Foundation for the Mid South believes that building wealth requires increased access to effective financial programs and information. When families possess the tools and knowledge to get their finances on track, they can begin to grow their savings, maximize their income, and acquire assets. The Foundation for the Mid South's goal to help families reach financial security is supported by two strategies:

- **Increasing financial competency**

We support activities that expand access to knowledge and resources to strengthen adult and youth financial competency.

- **Building assets**

We focus on expanding *Individual Development Accounts* (IDAs), which provide financial education while helping families save for and purchase an asset, like a business or home.

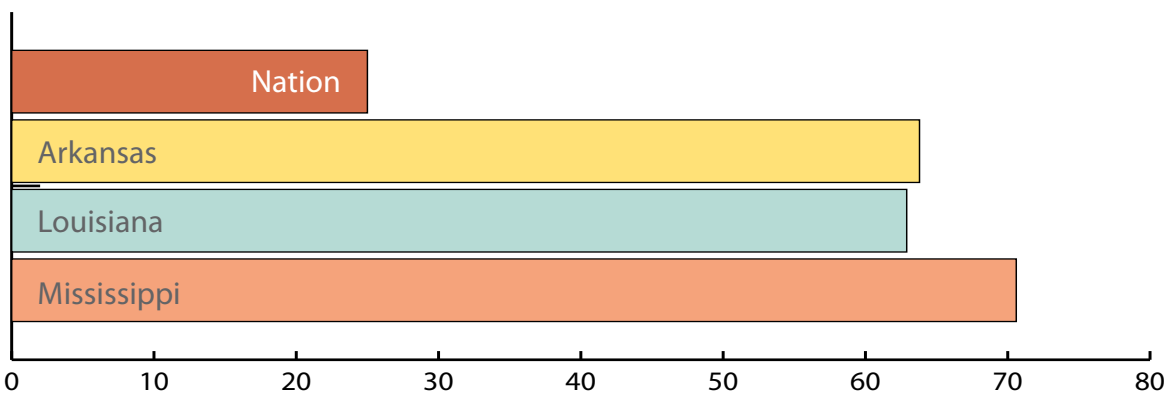
We also seek to increase the use of the *Earned Income Tax Credit* (EITC) among eligible low-wealth tax filers as a means to increase annual income. We encourage families to use the money earned from the federal tax credit specifically for savings or purchasing a transferable asset.

What is the earned income tax credit?

The Earned Income Tax Credit (EITC) was enacted in 1975 as a refundable tax credit targeting low- to moderate-income workers. It has become one of the most successful anti-poverty tools in the United States. Each year, an estimated five million people are lifted out of poverty and, in 2009, more than 24 million people received nearly \$50 billion in EITC.¹ The federal credit varies depending on family size, income and number of children, with an average return of \$2,600. As a result of the success of the federal credit, 22 states have enacted state EITC credits, providing an additional financial hand-up to those who need it most.

The Internal Revenue Service (IRS) indicates between 20 and 25 percent of eligible households do not claim the tax credit leaving billions of dollars unclaimed. Families in the Mid South are missing out on the tax credit at disturbingly higher rates. (See Figure 1) In the Mid South, 65% of eligible families do not claim the credit.

FIGURE 1 Percentage of Eligible Families Not Filing for EITC



Source: [Brookings Institute State Report creator](#)

Of this 65%, filers who are missing out include those who are:

- Living in rural areas
- Self-employed
- Disabled
- Childless
- Not proficient in English
- Older (grandparents)
- Recently divorced, unemployed, or experienced other changes to their marital, financial or parental status



How much money was left on the table?

Because such a large percentage of eligible families and individuals are not filing for the EITC, hundreds of thousands of people in Arkansas, Louisiana, and Mississippi are missing out on the financial benefits of the tax credit. In 2007, an estimated four billion dollars was left unclaimed.

TABLE 1

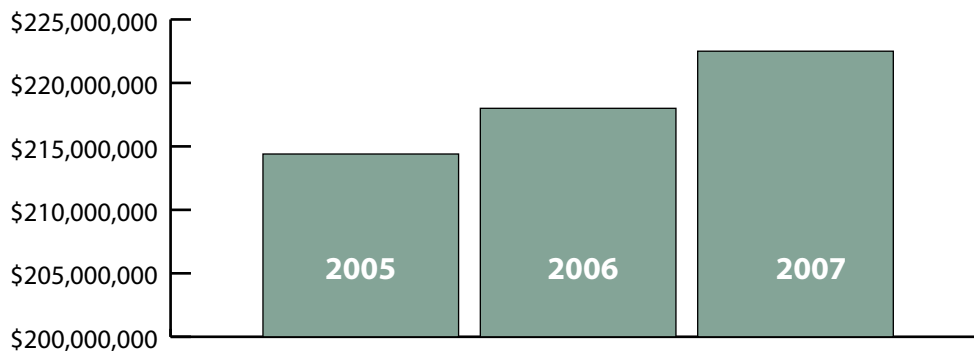
State	Sum of EITC Received	Number of EITC Tax Returns	Average Amount of EITC	Number of Eligible Filers who Did Not Claim EITC	Dollars Left Unclaimed (based on average EITC)
Arkansas	\$628,936,067	296,415	\$2,122	521,609	\$1,106,854,298
Louisiana	\$1,200,267,042	512,365	\$2,342	868,264	\$2,033,474,288
Mississippi	\$393,905,934	393,905	\$1,535	617,258	\$947,905,480
Total	2,223,109,043	1,065,330	\$5,999	2,007,131	4,088,234,066

Source: [Brookings Institute State Report creator](#)

In addition to dollars being lost to unclaimed credits, millions of dollars are also being lost to paid tax preparers in the forms of Refund Anticipation Loans (RALs) and Refund Anticipation Checks (RACs). (See Figure 2) These refund products are high interest check advances, which can cost a customer between \$100 and \$250. According to the IRS, the total cost associated with these products has increased each year and in 2007 over \$200 million dollars was lost in the Mid South alone.



FIGURE 2 **Dollars Lost to Paid Tax Services**



Source: [Brookings Institute State Report creator](#)

These figures represent dollars unnecessarily lost. The IRS has a program known as Volunteer Income Tax Assistance (VITA) to assist low- and moderate-income taxpayers, with incomes averaging below \$49,000, complete their annual tax returns for no cost at local community and neighborhood centers, libraries, schools, shopping malls, and other convenient locations. These programs provide free electronic filing and direct deposit which distributes refunds within a matter of days. Unfortunately, too many families and individuals are still not taking advantage of this service.

In the Mid South, less than 30% of all EITC returns were prepared by free services such as VITA sites. In order for families and individuals to take full advantage of their refund, access to and the use of VITA sites must increase.



MORE OPTIONS TO ENCOURAGE SAVING

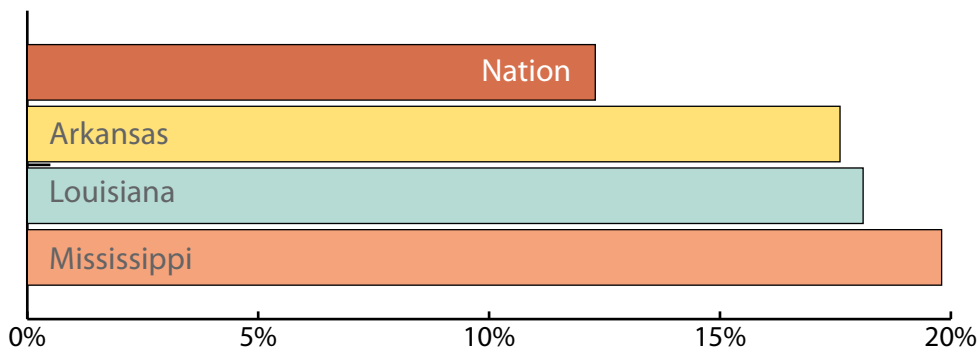
In addition to a high poverty rate, more than 35% of people in the Mid South are unbanked and do not have immediate access to savings opportunities.¹ Tax filers can now choose to split their refund into multiple parts, including savings accounts, IDAs, and savings bonds.

Why is the EITC important for the Mid South region?

Considering the billions of dollars left unclaimed and lost to paid tax preparers, the EITC has the potential to provide a significant economic boost to the region. In each state, local economies would benefit from the influx of cash each year. For example, the city of San Antonio estimates that each additional \$1 in EITC generates \$1.58 in local economic activity, and each \$37,000 results in one additional permanent job.²

For many low-income workers, the annual tax refund represents the largest single payment they will receive all year.² This tax refund is an opportunity to lift families out of poverty. In the Mid South, where more than 17 percent of all families live in poverty, the EITC can be a powerful tool to improve lives.

FIGURE 3 **Percentage of Families in Poverty**



Source: CFED 2009-2010 Assets and Opportunity Scorecard

Moving Forward

To increase the impact of this wealth building tool in the Mid South, promoting VITA and other free tax assistance sites is essential as we move forward.

The Foundation for the Mid South believes this wealth building tool will benefit both families and communities. Strategies that organizations can use to increase the impact of the Earned Income Tax Credit include the following:

- a) Increasing the awareness of the EITC and established VITA sites by keeping clients informed of EITC updates and eligibility requirements and the locations and hours of local VITA sites;
- b) Developing mobile VITA sites to reach rural areas and the elderly;
- c) Partnering with local colleges, universities, and faith-based groups to train tax preparers who are more familiar with the local community;
- d) Increasing the number of VITA sites with Spanish speaking tax assistants; and
- e) Increasing the number of sites in designated high-poverty areas.

The IRS provides online training for organizations and institutions wishing to become a VITA site. In addition, the National Credit Union Administration and the IRS have partnered to develop a step-by-step PowerPoint presentation which outlines the process in a user-friendly way. (See Additional Resources below for links)

As we approach the upcoming tax season, individuals can become trained preparers at a local VITA site, organizations can contact the IRS to start a VITA site, and everyone can spread the word about the credit. While we work to ensure more low-income families have access to and are aware of the free services available to them, we are also helping to create financially healthy communities. When families build wealth, the communities they live in become more stable and economically viable, as well.

Additional Resources

- IRS Link and Learn Training <http://www.irs.gov/app/vita/index.html>
- National Credit Union Administration [Establishing A Volunteer Income Tax Assistance \(VITA\) Site: How and Why](#)
- To find your local VITA site, visit: <http://www.irs.gov/individuals/article/0,,id=219171,00.html>

ENDNOTES

¹ Internal Revenue Service's website "EITC Central" found at <http://www.eitc.irs.gov/central/abouteitc/>.

Citation referenced November 2010.

² Berube, Alan. "Using the Earned Income Tax to Stimulate Local Economies". Citation referenced Oct. 10, 2010 from

<http://www.brookings.edu/metro/pubs/berube20061101eitc.pdf>

