

# A Working Families Credit for Washington State

by Andrea Lee and Remy Trupin

Thousands of families in Washington face daily challenges to making ends meet—low-wage incomes are insufficient to cover the high costs of healthcare, childcare, and job-related expenses. To make matters worse, these families pay higher percentages of their incomes in state and local taxes than wealthier residents.

A Working Families Credit will cut taxes for more than 350,000 Washington residents by adding 10 percent to their federal Earned Income Tax Credit (EITC) refund.

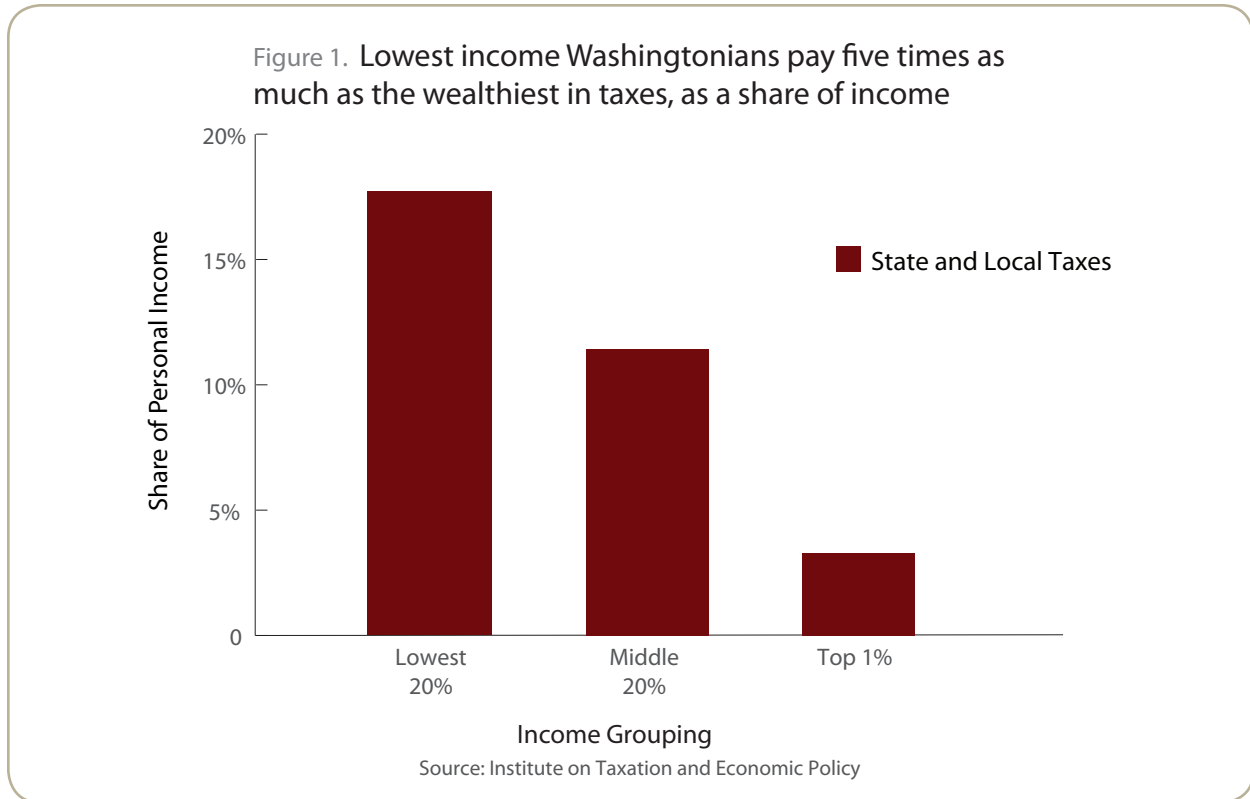
It will:

- Reduce sales and consumption taxes for low-wage workers by as much as 30 percent, mitigating the unfairness of Washington state's regressive tax structure.<sup>1</sup>
- Boost a minimum-wage worker's earnings by up to 31 percent when combined with the federal credit, supporting families who are working to move out of poverty.<sup>2</sup>
- Bring additional income to communities across the state, particularly rural areas and smaller towns.

Washington's Working Families Credit would build on the highly successful federal EITC, which in 2004 refunded nearly \$600 million to Washington residents.<sup>3</sup> Utilizing this existing program means we can ensure money is put back into the pockets of those who need it most, while keeping administration simple and inexpensive. Other states' experiences suggest that a state credit will increase the number of Washingtonians filing for the EITC, bringing additional money to local communities.

## **A boost for families who need it most**

The Working Families Credit creates an opportunity to bring more fairness to Washington's tax system by reducing taxes for lower-wage families. Washington's lowest-income residents pay five times more of their income to state and local government than wealthier residents contribute (Figure 1). Families balancing their budgets on less than \$17,000 a year spend nearly 18 percent of their income on taxes.<sup>4</sup>



The wealthiest pay just 3 percent of their income in taxes.<sup>5</sup> Other states have mechanisms in place to reduce taxes paid by their poorest residents, often exempting low-income households altogether.<sup>6</sup>

Another challenge lower-wage workers must confront is the loss of state-subsidized supports when they increase their income. Having to pay the high costs of unsubsidized healthcare, childcare and transportation—all while paying a disproportionate amount of tax—makes it harder for working families to make ends meet.

With the Working Families Credit, workers earning a full-time minimum wage are eligible for the maximum credit of \$470, depending on family

size. Many more workers—in occupations such as healthcare, childcare, and social services—who earn low wages above minimum wage also are eligible.

Households in the bottom 40 percent by income pay an average of about \$1,500 in sales and consumption taxes.<sup>7</sup> Households eligible for the maximum credit will see those taxes reduced by roughly 30 percent, an important step toward a more equitable tax structure. Also, like the EITC, the Working Families Credit amount increases with earnings, supporting working families' efforts.

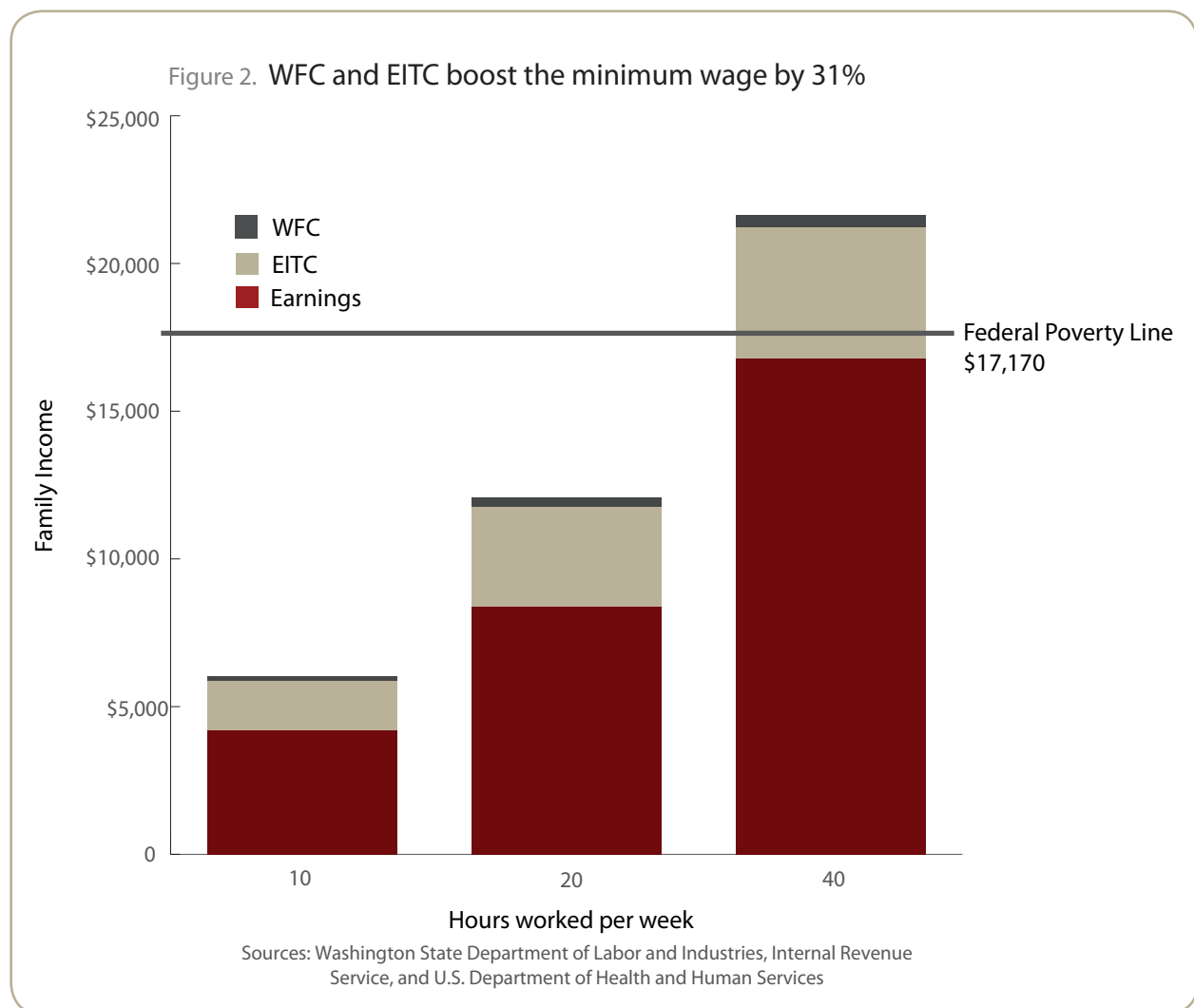
### Building on EITC's success

The federal Earned Income Tax Credit is widely hailed as a highly effective anti-poverty measure: in 2003, it lifted 4.4 million people above the poverty line.<sup>8</sup> But Washington's high cost of living and regressive tax structure potentially lessen the value of the EITC compared to many other states.

The Working Families Credit builds on the success of the federal EITC. At Washington's current

minimum wage of \$8.07, a full-time worker earns under \$17,000, below the poverty line for a family of three. The Working Families Credit, combined with the federal EITC, will boost this worker's minimum-wage earnings by 31 percent as well as reward a minimum-wage worker for more hours worked (Figure 2).<sup>9</sup>

The EITC promotes and supports work—a key to its broad bipartisan support. At the lower end of the wage scale, the EITC increases along with

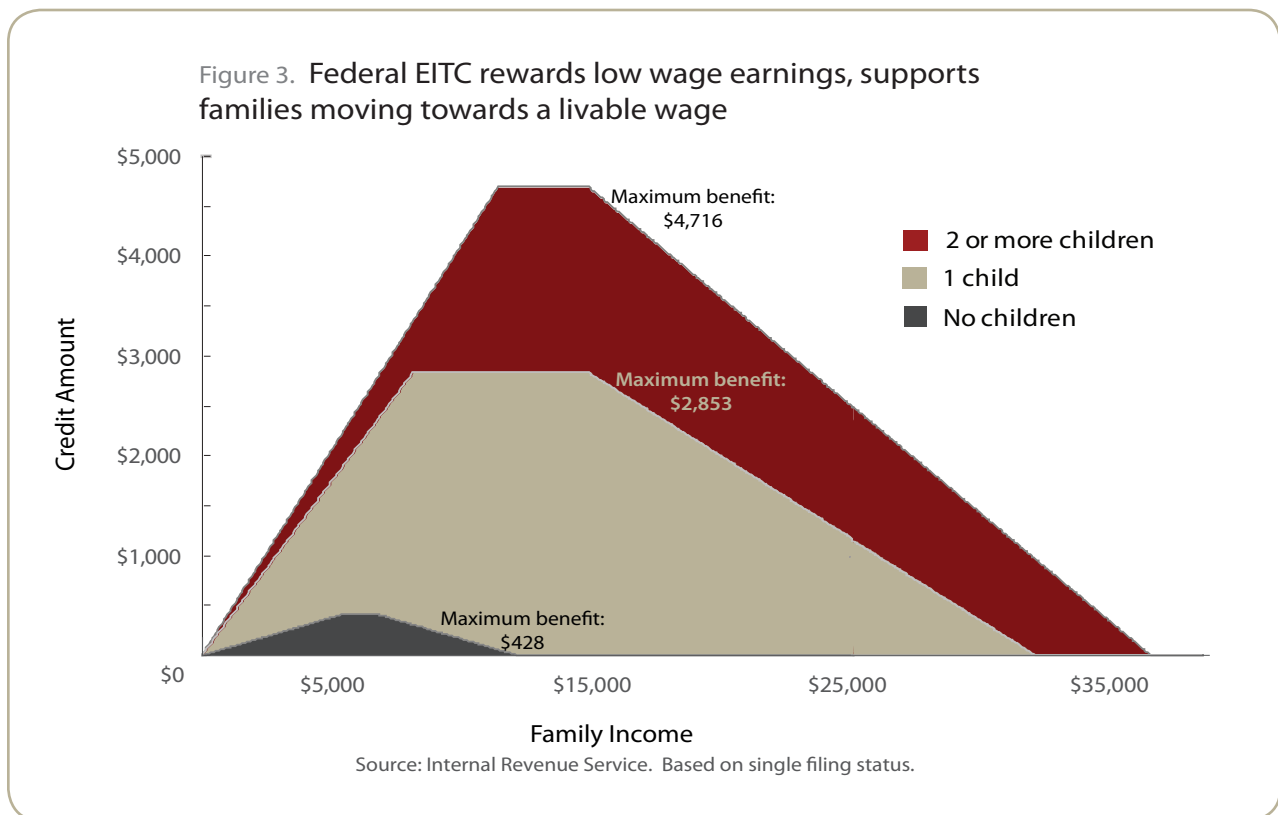


earnings (Figure 3). Evidence suggests that federal and state EITCs provide an important work support that increases parents' ability to enter the workforce.<sup>10</sup>

All Washington workers who receive the federal EITC will be eligible for the Working Families Credit. In 2004, more than 350,000 taxpayers in every district across Washington state received the EITC.<sup>11</sup> Districts with the highest percentages of Washington tax filers claiming the EITC are in rural and small metropolitan areas. One in four tax filers in the Yakima area (Legislative Districts 14 and 15) claimed the EITC.<sup>12</sup> Small cities also have large percentages of EITC claims; for example, 22 percent of tax filers in Spokane's District 3 claimed the EITC.<sup>13</sup> An estimate of Working Families

Credit recipients and the expected amount of their credits by legislative district is available in the Appendix.

Every community in Washington state benefits significantly from the federal EITC, an investment the Working Families Credit will expand. Other states' experiences suggest that it also will increase receipt of the federal credit, returning millions of federal tax dollars to Washington. To estimate the amount of taxes returned through the Working Families Credit, we multiply the total federal EITC claimed by Washington residents by the credit level, proposed here at 10 percent. Based on a 90 percent participation rate, the state credit would return \$57 million annually to Washington's working families.<sup>14</sup>



### Simple and inexpensive to administer

As noted, the Working Families Credit will be calculated at 10 percent of a family's federal EITC benefit. Two-thirds of the 23 states offering similar credits set their credits at this rate or higher.<sup>15</sup> Since the IRS is responsible for eligibility determination and the calculation of a family's base credit, only minimal administrative processing would be left to Washington's Department of Revenue.

Relying on IRS data for substantial administrative elements means the Working Families Credit can be implemented without a state income-tax structure. Key federal and state agencies can work together to administer the Working Families Credit: The IRS shares with states data concerning EITC recipients and credit amounts. Washington's Department of Revenue can use this data to alert families of their eligibility for the Working Families Credit and automatically generate applications.<sup>16</sup> Families simply sign and return the form to confirm their residency and accept their Working Families Credit; families residing in Washington for part of the year will be eligible for a proportional credit.

Other states and cities have successfully used IRS data to contact eligible families: Maryland automatically disbursed checks to people who received the federal EITC but not the state credit, while New York City uses the IRS data to identify residents who are eligible for federal, state, and local EITCs.<sup>17</sup>

Nevada, another state without an income tax, delivered millions of dollars in targeted tax cuts to its residents based on income eligibility in 2006 and spent only 3 percent of the program's cost on administration.<sup>18</sup> Since Nevada's program is similar to the Washington Working Families Credit's model, administration costs should be comparable.

### Families get opportunities to build assets

Simple features built into the Working Families Credit encourage families to build assets. By checking a box on the application, a family's credit can be deposited into a savings account or an Individual Development Account (IDA). If a family is eligible for certain programs, opting for an IDA can multiply the value of their credit: the United Way of King County's IDA initiative offers a 3-to-1 match for money saved toward education or homeownership and a 2-to-1 match to start or improve a business.<sup>19</sup> Even if families choose not to open an IDA, offering the option educates families about the importance of building assets.

San Francisco administers a Working Families Credit with an option for families to purchase U.S. Savings Bonds with their credits. In the initial pilot project, many families opted to purchase bonds with their credits and gift assets to their children or grandchildren.<sup>20</sup> San Francisco partners with the Federal Reserve Bank to deliver bonds within weeks of receiving a San Francisco Working Families Credit application, without collecting additional information from applicants.<sup>21</sup>

Other programs already in place in Washington also provide opportunities for families to build assets, including Guaranteed Education Tuition (GET), which allows parents to prepay their children's college tuition. Aligning asset-building programs with the Working Families Credit allows low-wage families to build their savings and work toward long-term financial success.

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## Conclusion

The Working Families Credit will provide an additional tax cut to low-wage workers and move Washington state toward a more equitable tax structure. Building on the success of the federal Earned Income Tax Credit, our state can ensure families who need the credit most can claim it easily, while keeping administrative costs low.

Washington state's Working Families Credit will put more money into communities, provide additional resources for asset-building, and boost a working parent's ability to build a better future for their family.

### Connect families through outreach

Supporting and expanding the availability of free tax preparation and other existing financial-stability and asset-building initiatives will efficiently connect eligible families with the Working Families Credit. Existing outreach efforts to promote the EITC can be easily expanded to educate families about the Working Families Credit.<sup>22</sup> A previous EITC outreach campaign costing \$316,000 brought Washington families an additional \$26 million in federal money, demonstrating additional EITC returns that will likely accompany outreach investments.<sup>23</sup> Additionally, a growing number of community-based organizations offer free income-tax preparation using volunteers trained and certified through the IRS-sponsored Volunteer Income Tax Assistance Program (VITA).

## Endnotes

1. According to analysis by the Institute for Taxation and Economic Policy, the poorest 40 percent of households pay about \$1,500 in sales and consumption taxes on average per year.
2. Full-time Washington state minimum wage in 2008 is \$16,786. A family with two children with married filing jointly tax status at this income is eligible for the maximum credits of \$4,716 (EITC) and \$471 (WFC), or 31% of \$16,786. EITC amount from IRS 1040 Instructions for 2007. <http://www.irs.gov/pub/irs-pdf/i1040.pdf> (accessed 14 January 2008).
3. The Brookings Institution. "EITC Zip Code Tax Return Data, 1997-2004." <http://www.brookings.edu/projects/eitc.aspx> (accessed 20 December 2007).
4. Institute for Taxation and Economic Policy. "Washington's tax system is the most regressive in the nation." 2003. <http://www.itepnet.org/wp2000/wa%20pr.pdf> (accessed 18 December 2007).
5. Ibid.
6. Jason Levitis and Jeremy Koulisch, "A Majority of States with Income Taxes have Enacted State Earned Income Tax Credits," Center on Budget and Policy Priorities. <http://www.cbpp.org/10-5-07sfp.htm> (accessed 20 December 2007).
7. See note 1.
8. Ami Nagle and Nicholas Johnson, "A Hand Up: How State Earned Income Tax Credits Help Working Families Escape Poverty In 2006," Center on Budget and Policy Priorities. <http://www.cbpp.org/3-8-06sfp.pdf> (accessed 18 December 2007).
9. See note 2.
10. V. Joseph Hotz, et al. (2006) "Examining the Effect of the Earned Income Tax Credit on the Labor Market Participation of Families on Welfare." National Bureau of Economic Research: Working Papers Series. <http://www.nber.org/papers/w11968> (accessed 20 December 2007).
11. The Brookings Institution. EITC Zip Code Tax Return Data, 1997-2004. <http://www.brookings.edu/projects/eitc.aspx> (accessed 20 December 2007).
12. Ibid.
13. Ibid.
14. Sloane Kuney and Jason Levitis, "How Much Would a State Earned Income Tax Credit Cost in 2008," Center on Budget and Policy Priorities. <http://www.cbpp.org/2-7-07sfp.htm> (accessed 20 December 2007).
15. This figure includes the District of Columbia.
16. Section 6103(d)(1) of the Internal Revenue Code addresses data sharing with state tax departments. [http://www4.law.cornell.edu/uscode/html/uscode26/usc\\_sec\\_26\\_00006103----000-.html](http://www4.law.cornell.edu/uscode/html/uscode26/usc_sec_26_00006103----000-.html) (accessed 12 December 2007).
17. Personal communication with James Parrott of the Fiscal Policy Institute. 18 December 2007.
18. Nevada Department of Administration, Division of Budget and Planning. 2007-2009 Executive Budget, Budget for the Health and Human Services Department. [http://budget.state.nv.us/budget\\_2007\\_09/2007\\_09\\_budget.htm](http://budget.state.nv.us/budget_2007_09/2007_09_budget.htm) (accessed 19 December 2007).
19. United Way of King County website, "Individual Development Account Program," <http://www.uwkc.org/ida/English/whatida.asp> (accessed 2 January 2008).
20. Federal Reserve Bank of San Francisco. Community Investments 17(2), May 2005. <http://www.frbsf.org/publications/community/investments/0505/mayissue.pdf> (accessed 11 January 2008).
21. Personal communication with Terri Feeley of SF Works. 20 December 2007.
22. The Department of Community, Trade, and Economic Development currently coordinates a statewide outreach campaign to increase participation in the federal EITC, including partnerships with twelve local EITC outreach campaigns during the 2006 tax year. <http://cted.wa.gov/DesktopModules/CTEDPublications/CTEDPublicationsView.aspx?tabID=0&ItemID=4673&Mid=846&wversion=Staging#art3> (accessed 11 January 2008).
23. Office of Governor Gary Locke, News Release. "Washington Leads Nation in Growth of EITC applicants." <http://www.digitalarchives.wa.gov/governorlocke/press/press-view.asp?pressRelease=624&newsType=1> (accessed 23 December 2007).

## Appendix: Working Families Credit amounts by Washington state legislative district

District	Tax returns claiming EITC	Percentage claiming EITC	Total EITC received	Average EITC amount	Average WFC amount
<b>Statewide</b>	<b>350,241</b>	<b>12.7%</b>	<b>\$584,204,725</b>	<b>\$1,668</b>	<b>\$167</b>
District 1	4,530	7.8%	\$6,802,893	\$1,502	\$150
District 2	8,227	14.1%	\$14,104,152	\$1,714	\$171
District 3	10,882	21.6%	\$18,479,319	\$1,698	\$170
District 4	8,704	14.7%	\$14,897,289	\$1,712	\$171
District 5	3,266	5.0%	\$4,905,958	\$1,502	\$150
District 6	6,683	11.8%	\$11,130,742	\$1,666	\$167
District 7	9,620	19.0%	\$17,108,526	\$1,779	\$178
District 8	7,633	13.7%	\$13,763,344	\$1,803	\$180
District 9	7,014	14.7%	\$12,178,672	\$1,736	\$174
District 10	6,795	11.4%	\$10,970,709	\$1,614	\$161
District 11	8,307	14.2%	\$13,759,181	\$1,656	\$166
District 12	9,206	17.7%	\$16,874,819	\$1,833	\$183
District 13	9,122	18.8%	\$16,880,975	\$1,851	\$185
District 14	10,372	20.8%	\$19,858,604	\$1,915	\$191
District 15	12,427	27.1%	\$25,056,671	\$2,016	\$202
District 16	9,299	17.6%	\$17,803,781	\$1,915	\$191
District 17	7,710	13.3%	\$13,510,241	\$1,752	\$175
District 18	6,107	10.3%	\$10,232,216	\$1,675	\$168
District 19	8,387	16.8%	\$14,619,206	\$1,743	\$174
District 20	8,205	15.2%	\$13,948,464	\$1,700	\$170
District 21	6,626	10.7%	\$10,559,865	\$1,594	\$159
District 22	7,301	11.6%	\$11,250,771	\$1,541	\$154
District 23	5,549	9.7%	\$8,827,123	\$1,591	\$159
District 24	8,015	14.0%	\$12,907,917	\$1,610	\$161
District 25	6,951	11.3%	\$11,427,426	\$1,644	\$164
District 26	5,850	10.5%	\$9,439,589	\$1,614	\$161
District 27	7,213	14.4%	\$12,040,196	\$1,669	\$167
District 28	8,968	16.7%	\$15,816,993	\$1,764	\$176
District 29	10,900	21.1%	\$19,349,077	\$1,775	\$178
District 30	7,324	13.8%	\$12,920,682	\$1,764	\$176
District 31	6,009	10.8%	\$9,939,953	\$1,654	\$165
District 32	4,106	7.3%	\$5,578,285	\$1,359	\$136
District 33	8,580	15.1%	\$14,670,900	\$1,710	\$171
District 34	5,659	9.8%	\$8,462,099	\$1,495	\$150
District 35	7,420	13.7%	\$12,315,881	\$1,660	\$166
District 36	3,793	5.4%	\$3,408,497	\$899	\$90
District 37	8,515	15.7%	\$13,191,379	\$1,549	\$155
District 38	7,735	14.0%	\$12,406,117	\$1,604	\$160
District 39	6,774	12.3%	\$11,120,967	\$1,642	\$164
District 40	7,066	12.6%	\$11,255,952	\$1,593	\$159
District 41	3,374	5.3%	\$4,675,292	\$1,386	\$139
District 42	8,010	13.1%	\$12,784,485	\$1,596	\$160
District 43	4,377	6.6%	\$3,737,290	\$854	\$85
District 44	5,258	9.2%	\$8,385,105	\$1,595	\$159
District 45	3,033	5.2%	\$4,170,017	\$1,375	\$137
District 46	4,331	7.1%	\$5,061,596	\$1,169	\$117
District 47	6,710	11.9%	\$11,567,713	\$1,724	\$172
District 48	3,453	5.6%	\$4,816,738	\$1,395	\$139
District 49	8,845	15.9%	\$15,231,055	\$1,722	\$172

Source: The Brookings Institution, 2004 EITC Zip Code Tax Return Data.