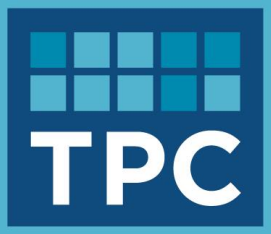

TAX POLICY CENTER
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BOOSTING WAGES OR HELPING CHILDREN? UNDERSTANDING HOW NEW EARNINGS AND CHILD TAX CREDIT PROPOSALS IMPACT INCOME INEQUALITY AND VULNERABLE CHILDREN

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ABSTRACT

The earned income tax credit (EITC) and child tax credit (CTC) provide substantial benefits to working families with children. The EITC also provides modest benefits to workers without custodial children, often called "childless workers" for tax purposes. Together, the credits lift almost 9 million people out of poverty each year. We analyze the Working Families Tax Relief Act (WFTRA), the LIFT (Livable Income for Families Today) the Middle Class Act (LIFT Act), the American Family Act (AFA), and the Cost-of-Living Refund (CLR), all recent proposals to extend the EITC and CTC. For each proposal, we focus on fiscal cost and the distribution of benefits and analyze multiple alternatives to these proposals to better understand the inherent trade-offs between how expansive a proposal is, its cost, and how targeted the benefits will be.

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The Urban-Brookings Tax Policy Center aims to provide independent analyses of current and longer-term tax issues and to communicate its analyses to the public and to policymakers in a timely and accessible manner. The Center combines top national experts in tax, expenditure, budget policy, and microsimulation modeling to concentrate on areas of tax policy that are critical to future debate.

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INTRODUCTION

The earned income tax credit (EITC) and child tax credit (CTC) provide substantial benefits to working families with children.[i] The EITC also provides modest benefits to workers without custodial children, often called "childless workers" for tax purposes.[ii] Because the amount of credit childless workers can qualify for is modest, almost all benefits from both credits flow to families with children. Together, the credits lift almost 9 million people out of poverty each year (Fox 2019).

Policymakers are looking to build on the success of these credits and further address both (a) income inequality between very high–income people and everyone else (Congressional Budget Office 2019), which is fueled in part by wage stagnation (Mishel, Gould, and Bivens 2015), and (b) relatively poor outcomes for low-income children (Duncan, Ziol-Guest, and Kalil 2010; Ratcliffe 2015). And given the CTC increase enacted in 2017 is set to expire after 2025, legislators are considering the next phase of work and child subsidies.

In this report, we analyze four large-scale proposals that were introduced in 2019:

- the Working Families Tax Relief Act, or WFTRA, introduced by Senators Bennet (D-CO), Brown (D-OH), Durbin (D-IL), and Wyden (D-OR);
- the LIFT (Livable Incomes for Families Today) the Middle Class Act, or LIFT Act, introduced by Senator Harris (D-CA);
- the American Families Act, or AFA, introduced by Senators Bennet (D-CO) and Brown (D-OH) and Representatives DelBene (D-WA) and DeLauro (D-CT); and
- the Cost-of-Living Refund, or CLR, introduced by Senator Brown (D-OH) and Representatives Khanna (D-CA), Watson-Coleman (D-NJ), and Tlaib (D-MI).

Options for modifying the earnings and child tax credits can be evaluated along many dimensions, such as work incentives, marriage penalties, simplicity, and administrability, as described by Maag, Marron, and Huffer (2019). For each proposal, we focus on total fiscal cost and the distribution of benefits to see how well it either reduces income inequality or provides additional resources to low-income families with children.

In the proposals we analyze, policymakers essentially consider three choices: increasing the child tax credit, which focuses on alleviating relatively poor outcomes for low-income children; increasing the EITC for households with children, which focuses on reducing income inequality for families with children; and increasing the EITC for childless workers, which focuses on reducing income inequality for a portion of the population largely excluded from current tax benefits.

Like the EITC and CTC, all the proposals analyzed in this report would provide benefits to both families with children and those with very low incomes, illustrating that a proposal can focus on one goal while still

accomplishing others, a concept we discuss in detail. However, the focus affects how broad the policy will be and how much the proposal will cost. For instance, a policy focused on low-income children could reduce income inequality and improve outcomes for children but not affect income inequality among people without children.

As policymakers make decisions, they must keep in mind that any effort to increase the relative benefits for one group inevitably means a decrease in the relative benefits (though not necessarily the absolute benefits) for other groups. If, for example, the childless EITC were expanded and otherwise unchanged, the share of total EITC benefits going to families with children would decline even though the absolute level of benefits going to families with children would not change. Later in the report, we modify important parameters of each proposal to illustrate how different choices would alter these trade-offs.

HOW THE TCJA TEMPORARILY AFFECTED TAX BENEFITS FOR WORK AND FAMILY

Before the Tax Cuts and Jobs Act of 2017 (TCJA), both Republicans (such as Paul Ryan, then Speaker of the House) and Democrats (such as President Obama) had proposed expanding the "childless" EITC (Executive Office of the President and US Treasury Department 2014).[iii] The TCJA, however, left the EITC (and thus the incomes of low-income childless families) largely unchanged. That is, the TCJA delivered an average annual tax cut of $1,610 (across all families) at a cost of $1.9 trillion over the 10-year budget window, but childless families in the bottom one-fifth of the income distribution saw their taxes decline by an average of about $25 in 2018 relative to prior law (Congressional Budget Office 2018).[iv] Very low–income families without children generally do not owe federal income tax so do not benefit from reduced tax rates.

Families with children generally fared better under the TCJA. Those in the lowest one-fifth of the income distribution saw their taxes drop, on average, by $210 in 2018. In part, this was because the law changed how families are taxed (Maag 2019). The TCJA temporarily increased the maximum benefit from the CTC from $1,000 per qualifying child under age 17 to $2,000 per qualifying child under age 17; it also increased the income range eligible for benefits. Up to $1,400 of this credit could be received as a refund (up from $1,000 under prior law but still less than the full amount of the credit). Other dependents became eligible for a new $500 nonrefundable credit. These changes maintained the tax code's recognition that families raising children have less ability to pay tax than those not raising children. Offsetting some of these changes, the TCJA temporarily eliminated the personal exemption for dependents, a tax benefit that allowed families to exempt from taxation a fixed amount of income for each child and other dependents.

Additional changes in the TCJA included increasing the standard deduction (which allows taxpayers to exempt a fixed amount of income based on whether the tax unit is a single person, a single parent, or a married couple filing a joint return), limiting certain itemized deductions, and reducing tax rates. Most of these changes did not further increase benefits or reduce taxes for low-income families.

Almost all the changes in the TCJA directed at individuals are scheduled to expire at the end of 2025, limiting the fiscal cost of the bill but raising the likelihood that additional legislation might continue some of the "temporary" changes or spur new tax policies directed at low- and middle-income workers, families with children, or both.

We use the Tax Policy Center's microsimulation model to describe current benefits from the CTC and EITC for families with and without children. Estimates from proposals that follow build on these existing benefits.

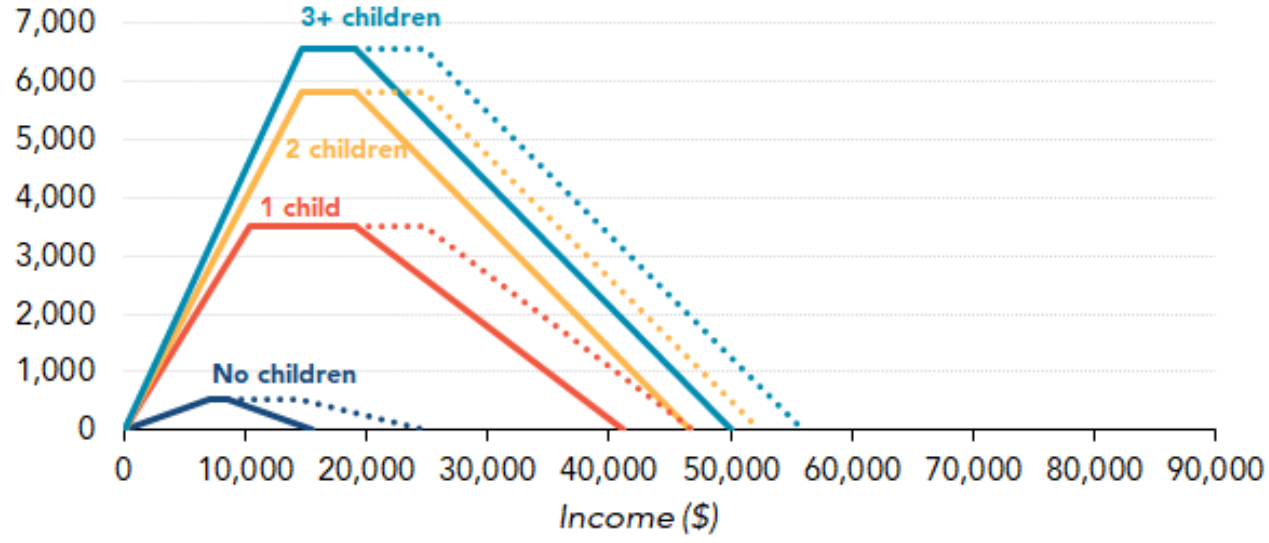
THE EARNED INCOME TAX CREDIT

The EITC benefits low- and moderate-income working families by providing them with a tax credit equal to a fixed percentage of earnings, starting with their first dollar of earnings until the credit reaches its maximum (figure 1). The credit rate varies based on the number of children in the family. For a single worker with one child, for example, the credit increases by 34 cents for each additional dollar of earnings until it reaches a maximum of around $3,500, which represents earnings of a bit more than $10,000. The maximum credit is paid until earnings or income reach a higher threshold, at which point the credit begins to phase out. For a worker with one child, any income above roughly $19,000 reduces their credit by about 16 cents for each dollar of additional income. Workers with one child receive no credit once their income reaches roughly $41,100. Married couples can earn about $6,000 more than single people before their benefits begin to phase out. Otherwise, the EITC does not vary based on marital status. Workers with two or three qualifying children have a higher credit rate and can receive a larger maximum credit. Workers with no children have a lower credit rate and much smaller maximum credit.

The EITC is refundable. This means that workers receive the full value of the credit regardless of how much income tax they owe. The credit first offsets any income taxes owed; any additional amount a person qualifies for will be paid out as a tax refund along with any other tax refund amounts the worker might be owed.

FIGURE 1

Earned Income Tax Credit, 2019



Source: Urban-Brookings Tax Policy Center.
Note: Assumes all income comes from earnings. Dotted lines represented married couples.

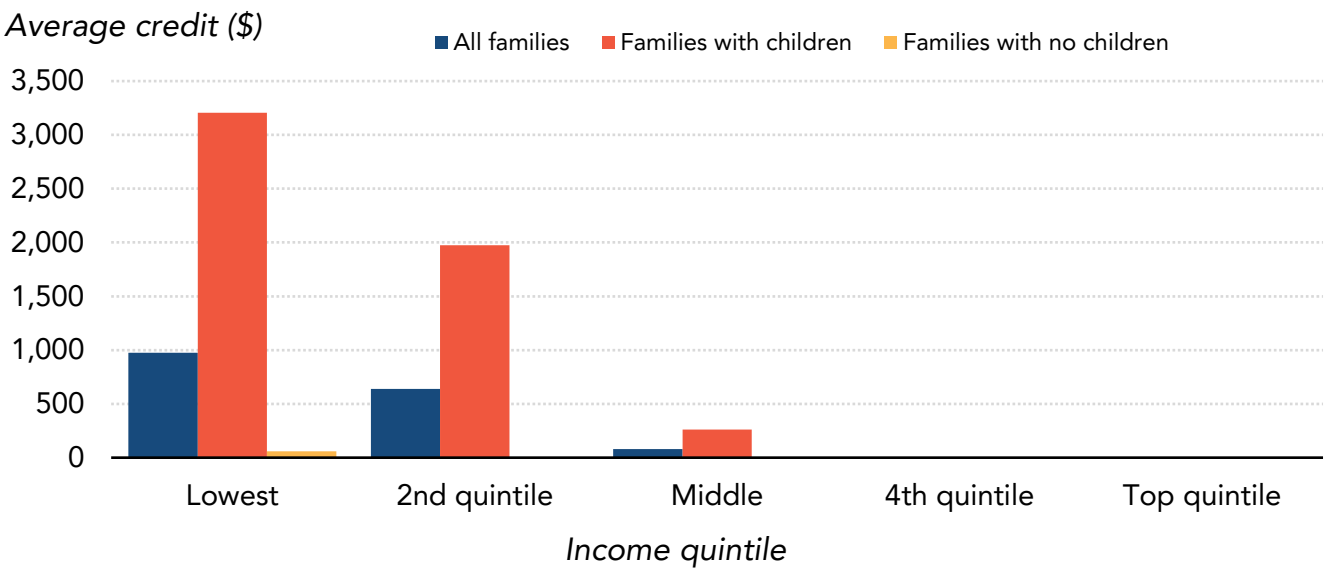
Each year, the maximum amount of income eligible for the credit and the point where the credit begins to phase out increase with inflation. The pace of those future increases was slowed by the TCJA, which indexes most income tax parameters to the chained consumer price index for urban consumers, a price index that typically increases more slowly than the regular consumer price index for urban consumers.

About 15 percent of all families benefit from the EITC. Among families with children, 37 percent of families receive benefits from the credit.[v] Families with children receive the highest average benefits, and these decline as income increases (figure 2). Families with no custodial children receive very small benefits from the EITC. Across all groups, families in the lowest income quintile (i.e., the bottom 20 percent) receive the largest average benefits.

FIGURE 2

Average EITC Benefits, 2019

Families with children versus families without children



Source: Tax Policy Center microsimulation model 0319-1.
Note: Each quintile represents families in a 20 percent segment of the income distribution. Lowest quintile

THE CHILD TAX CREDIT

The CTC grants taxpayers a credit of up to $2,000 for each child under age 17 who is a citizen. Typically, the child must reside with the taxpayer, though this rule has some exceptions. The CTC is partially refundable: if the credit exceeds taxes owed, taxpayers can receive up to $1,400 per child of the balance as a refund, known as the additional child tax credit (ACTC) or refundable CTC. Benefits of the ACTC are calculated as 15 percent of

earnings above $2,500. For the most part, the CTC is not indexed for inflation, so the real value of this benefit will decline over time. How much of the credit can be received as a refund is indexed for inflation. The credit is reduced by 5 percent of adjusted gross income above $200,000 for single parents and $400,000 for married couples (figure 3).

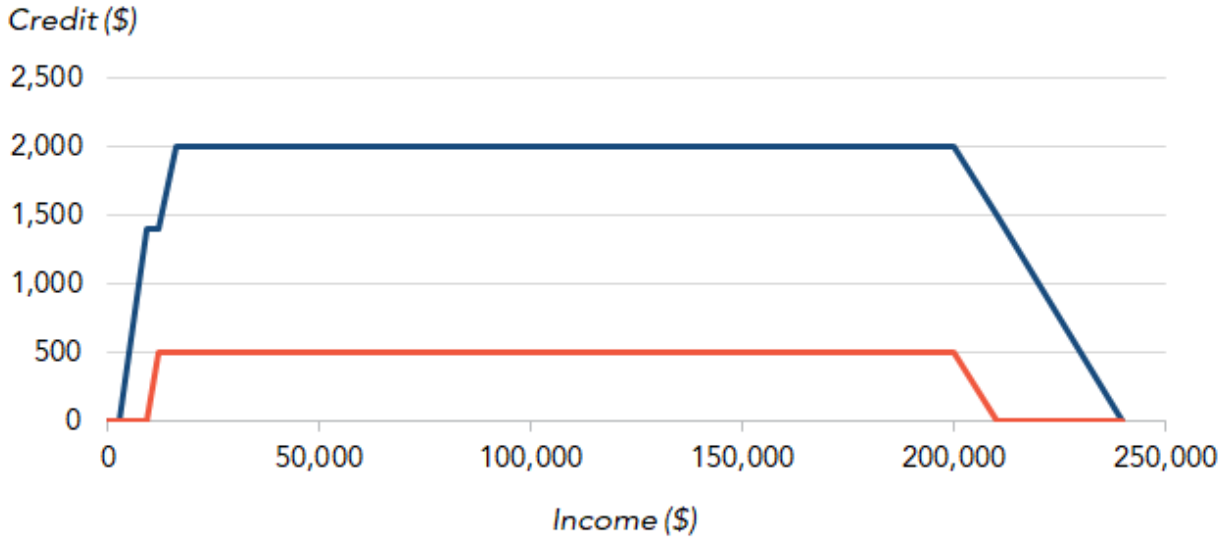
The CTC also provides a parallel $500 nonrefundable credit to dependents who are not eligible for the $2,000 CTC, known as the credit for other dependents. Before 2018, these individuals would not have qualified for a CTC but would have qualified for a personal exemption for dependents. Dependents who now qualify for the other dependent credit include children ages 17 to 18, children ages 19 to 23 and in school full time in at least five months of the year, and older dependents.

About 90 percent of families with children receive a benefit from the CTC. Those not receiving a benefit are families with no earnings, with earnings under $2,500, or with incomes too high to benefit from the credit. This phase-in for nontaxpayers indicates that Congress wanted to focus the credit on workers with children, not all families with children. Some reform proposals seek to shift the credit's focus and make it fully refundable, even to those who do not work in the paid labor force during the year.

FIGURE 3

Child Tax Credit, Single Parent

One child, 2019



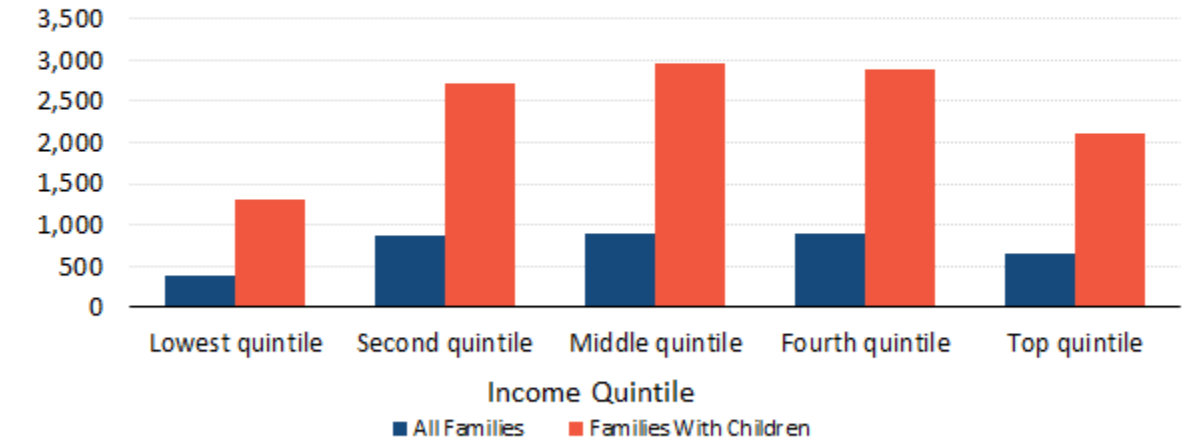
Source: Urban-Brookings Tax Policy Center calculations.
Note: Assumes all income comes from earnings, and child meets all tests to be a CTC-qualifying dependent. Credit for married parents begins to phase out at $400,000 of income. Only citizen children qualify for the $2,000 CTC for children under 17. Noncitizens under age 17 who meet the dependency tests of eligibility can qualify for the credit for other dependents.

On average, families with children in the lowest income quintile receive $1,304 from the CTC. Families with children in the top two income quintiles receive benefits averaging over $2,900 (figure 4). Benefits can average more than $2,000 because more than one child in a family can be eligible for the CTC.

FIGURE 4

Average CTC Benefits, 2019

All families and families with children



Source: Tax Policy Center microsimulation model version 0319-1.
Note: Each quintile represents families in a 20 percent segment of the income distribution. Lowest quintile represents families in the lowest 20 percent of the income distribution.

COMPARING THE EARNED INCOME TAX CREDIT AND THE CHILD TAX CREDIT

The primary differences between the EITC and the CTC are that (a) the CTC is available to taxpayers with much higher incomes than the EITC is; (b) workers must earn at least $2,500 to be eligible for CTC benefits; and (c) the size of the CTC scales for many families proportionately with the number of children, whereas the EITC provides the largest per child benefit for families with one child, with decreasing amounts for second and third children and no additional benefit for more than three children.

The EITC encourages many people to work because only people who are working can receive the credit, and the credit phases in as income increases. The 1975 legislation establishing the credit was intended to offset payroll taxes and offer an alternative to the then-prevailing welfare program, Aid to Families with Dependent Children, which gave the highest benefit to nonworkers. Since its inception, the EITC has been expanded many times, for many offsetting far more than payroll taxes; the largest expansions occurred through legislation in 1986, 1990, and 1993.

Unlike Aid to Families with Dependent Children (the predecessor to Temporary Assistance for Needy Families) and some other in-kind transfer programs that were criticized for reducing work incentives among single mothers (Moffitt 1992) and some married couples (Hoynes 1996), analyses of the EITC shows that the net

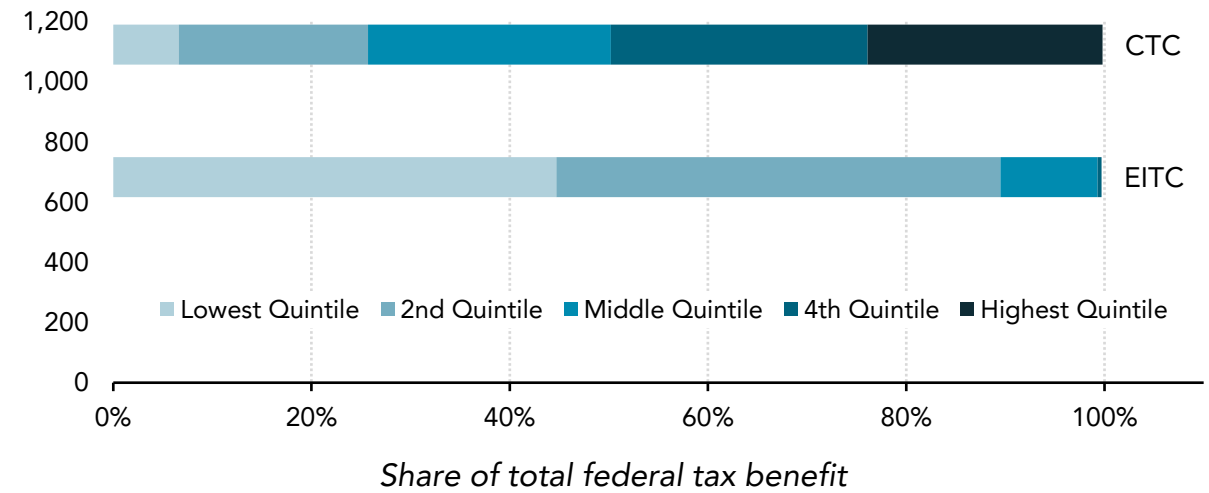
effect of the credit is to encourage people to work (Eissa and Liebman 1996; Meyer and Rosenbaum 2001). This is particularly true among single parents, many of whom are eligible for the EITC. Very few studies of how the CTC affects labor supply have been conducted, but the goal of the CTC (particularly the current incarnation, which provides benefits, as did the personal exemption for dependents, relatively high up the income scale) may be simply to support families with children. Further, tax law has always recognized that families of different sizes have different abilities to pay taxes. For instance, at $75,000 of income, a one-person family may be able to live better while paying more taxes than an equal-income family of four, whose average income per person is $18,750. The CTC can be thought of as an adjustment for ability to pay taxes based on family size.

Over the 10-year budget window, the current-law EITC will deliver about $700 billion in benefits. Almost 90 percent of benefits from the EITC go to workers in the bottom 40 percent of the income distribution (figure 5).

Over the 10-year budget window, the current-law CTC will deliver about $1.1 trillion in benefits. Less than 10 percent of all benefits go to families in the bottom 20 percent of the income distribution, and almost half of all benefits from the CTC go to families in the top 40 percent of the income distribution (figure 5).

FIGURE 5

Distribution of Total EITC and CTC Benefits, 2019
By income quintile



Source: Tax Policy Center microsimulation model version 0319-1, Tables T19-0026 (EITC) and T19-0062 (CTC).
Note: Expenditures estimated over fiscal years 2019-2028. Each quintile represents families in a 20 percent segment of the income distribution. Income for quintiles is defined as expanded cash income.

Ignoring the EITC's employment effects and treating the EITC and CTC as cash benefits in the supplemental poverty measure, the EITC and CTC lift more people out of poverty than any other means-tested program (Fox

2019). They do this in large part because they are refundable (taxpayers can receive the entire EITC for which they qualify, even if they owe no income tax or less than their EITC. Taxpayers can receive up to $1,400 per child under age 17 as a refundable CTC).

WORK AND FAMILY PROPOSALS

Several members of Congress and one-time Democratic presidential hopefuls have designed proposals that would use the tax code to further assist low- and moderate-income workers and families with children. These proposals, coupled with several major provisions affecting families being set to expire after 2025, make future changes to these aspects of the tax code seem likely. To date, these proposals call for broad expansions to work and family tax credits, but they have been largely proposed or discussed separate from conversations about how to offset their costs. Obviously, significant new revenue losses would further increase future budget deficits, which could force Congress to consider adjustments to these types of proposals.

We examine four major proposals and estimate their cost over the 10-year budget window from fiscal years 2019 to 2028. Given concerns about income inequality and poor outcomes for lower-income children, we focus on how the various proposals will affect people in the bottom quintile of the income distribution, noting the differences among families with and without children. We also consider the total revenue costs of the proposals. These distributional and revenue results reveal some of the types of trade-offs every proposal must consider.

All the proposals we examine satisfy several goals, including reducing income inequality and providing additional resources for families with children. All the policies, whether oriented more toward children or work, will support many families with children in the bottom quintile of the income distribution because many parents work.

Because the current CTC provides benefits for almost all families with children, policies that simply augment this credit tend to be more expensive and provide benefits further up the income distribution than a policy that focuses only on low-income children. Child-focused policies will not address income inequality for families without children.

Policies that focus on increasing the benefits of work can ultimately provide benefits to people with higher incomes than the existing EITC because at any given phase-out rate, it takes higher levels of income for the benefit to eventually be eliminated. Thus, simple EITC benefit expansions also tend to rise further up the income distribution (though not as far as CTC benefit expansions). The analysis we provide helps portray these inevitable trade-offs in cost, efficiency, and equity.

Here we provide a brief summary of each proposal, including a figure that illustrates the benefits (highlighting existing benefits in gray). We provide additional details about each proposal in a concluding table (table 1).

THE LIFT THE MIDDLE CLASS ACT

Senator Kamala Harris (D-CA) proposes to raise the incomes of working families through a new tax proposal called the LIFT (Livable Incomes for Families Today) the Middle Class Act, which would add a new worker credit on top of the existing EITC. This new refundable tax credit would match up to $3,000 of earnings for single people and $6,000 for married couples (figure 6 and table 1) who are at least 18 years old. Students who receive Pell grants could consider those grants as earnings when calculating their credit. The bill is designed primarily to reduce income inequality.

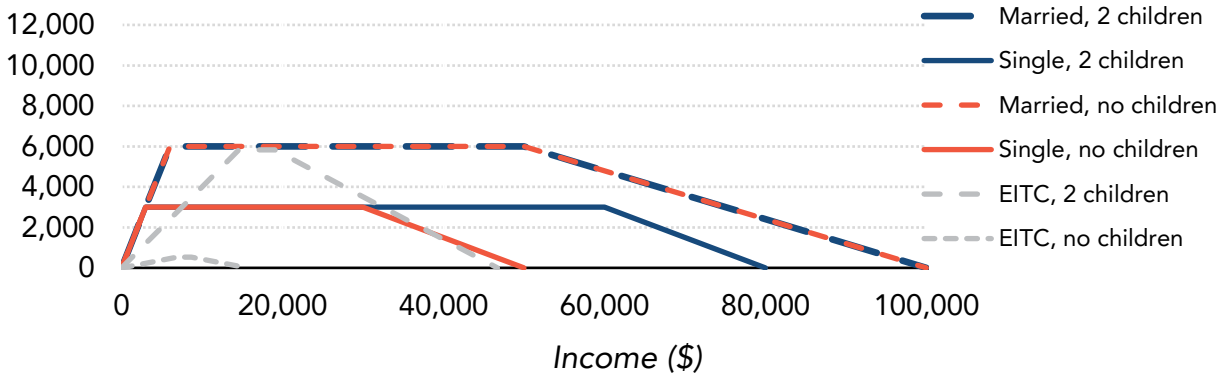
Unlike other credits designed to reward work (including the EITC), this new tax credit would deliver substantial benefits to workers without children at home. Unlike proposals to expand the childless portion of the EITC, it supports workers with low earnings who marry other low earners (rather than potentially increasing the marriage penalties for such workers).

Because the credit is based on income and marital status but not the number of children a person has, it should be more predictable to many people. This could make make the credit easier to claim regularly throughout the year, which could help stabilize volatile incomes. Unlike the other proposals analyzed in this report, the LIFT Act benefits would supplement existing tax credits (figure 7). The LIFT Act does not change the CTC.

FIGURE 6

LIFT Act

Credit by filing status and number of children

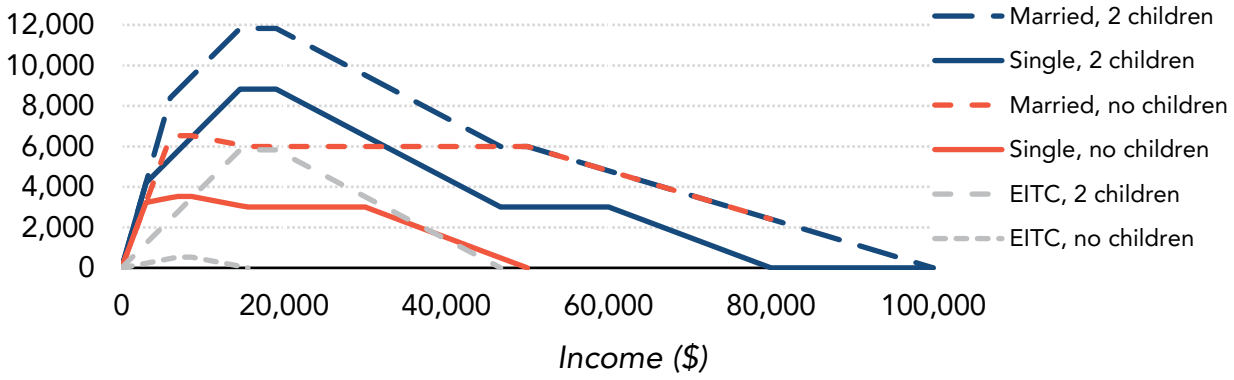


Source: Authors' calculations.
Note: LIFT credit would supplement, not replace, existing EITC for eligible families. These calculations assume all income comes from earnings.

FIGURE 7

LIFT Credit Plus Existing EITC

Credit by filing status and number of children



Source: Authors' calculations.
Note: LIFT credit would supplement, not replace, existing EITC for eligible families. These calculations assume all income comes from earnings.

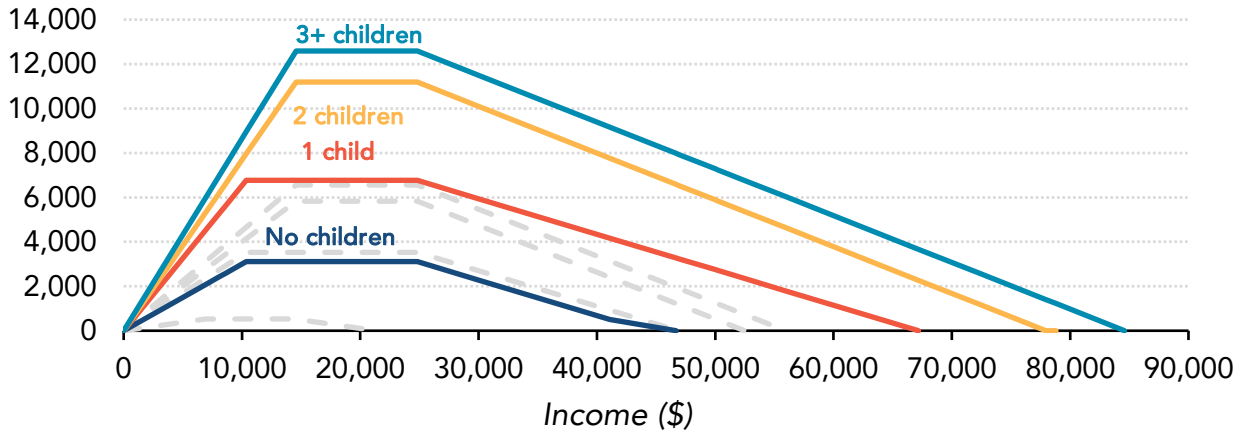
COST-OF-LIVING REFUND

Senator Sherrod Brown (D-OH) and Representatives Ro Khanna (D-CA), Bonnie Watson-Coleman (D-NJ), and Rashida Tlaib (D-MI) have proposed an expansion of the EITC called the cost-of-living refund (CLR). A similar bill was previously introduced as the Grow American Incomes Now (GAIN) Act. The CLR was designed to help make up for slow wage growth experienced by workers over the past generation. Sponsors discussed how much the EITC would have needed to grow so that the combination of the EITC and wages at the bottom of the income distribution would have grown as much as income grew for those with very high incomes. The bill would roughly double EITC benefits for families with children and increase benefits as much as six-fold for workers without children (figure 8 and table 1). Importantly, the bill would aid people with higher incomes more than the current law does simply because increasing the maximum credit (while maintaining the phase-out rate) means the credit would take longer to phase out. The bill would allow EITC filers to claim a $500 advance payment on their credit once a year (before filing a tax return). The CLR would not alter the CTC.

FIGURE 8

Cost-of-Living Refund

Impact on EITC for married couples



Source: Authors' calculations.
Note: Dotted lines represent current law EITC for married taxpayers. Credit phases out $5,790 earlier for single taxpayers. These calculations assume all income comes from earnings.

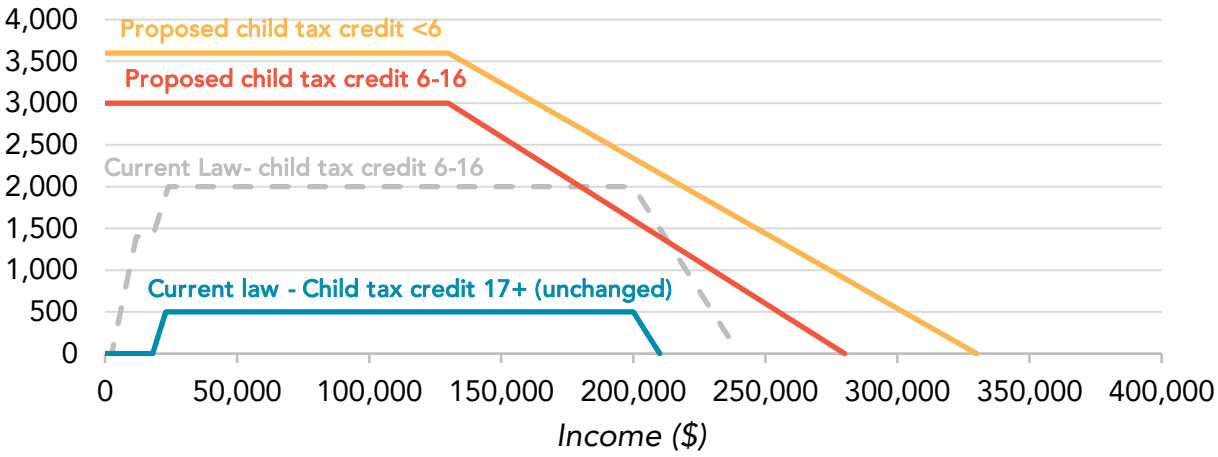
AMERICAN FAMILY ACT

Senators Michael Bennet (D-CO) and Sherrod Brown (D-OH) and Representatives Rosa DeLauro (D-CT) and Suzan DelBene (D-WA) propose to expand the CTC for all children under age 17 and add a bonus for families with children under age 6. The American Family Act (AFA) aims to lift more children out of poverty and provide a substantial benefit for even very low–income children and would do so by increasing the CTC in two ways. It would increase the maximum credit for children ages 6 to 16 from $2,000 per child to $3,000 per child and further increase the credit for children under age 6 to $3,600. It would also provide the full benefit to low-income families, regardless of earnings, by making the credit fully refundable. The AFA would not alter the $500 nonrefundable portion of the CTC for dependents not eligible for the CTC. Just as under current law, this $500 credit would expire after 2025. However, the credit for families with children under age 17 would start phasing out at a lower income threshold than under current law, at a rate of 2 percent for families with one child and income over $130,000 ($180,000 if married). That rate would increase by 2 percentage points for each additional child (figure 9 and table 1). The AFA would not alter the current-law EITC.

FIGURE 9

American Families Act, Single Parent

One child, 2019



Source: Urban-Brookings Tax Policy Center calculations.
Note: Assumes all income comes from earnings, and child meets all tests to be a CTC-qualifying dependent. Credit for married parents begins to phase out at $400,000 of income. Only citizen children qualify for the $2,000 CTC for children under 17. Noncitizens under age 17 who meet the dependency tests of eligibility can qualify for the credit for other dependents.

WORKING FAMILIES TAX RELIEF ACT

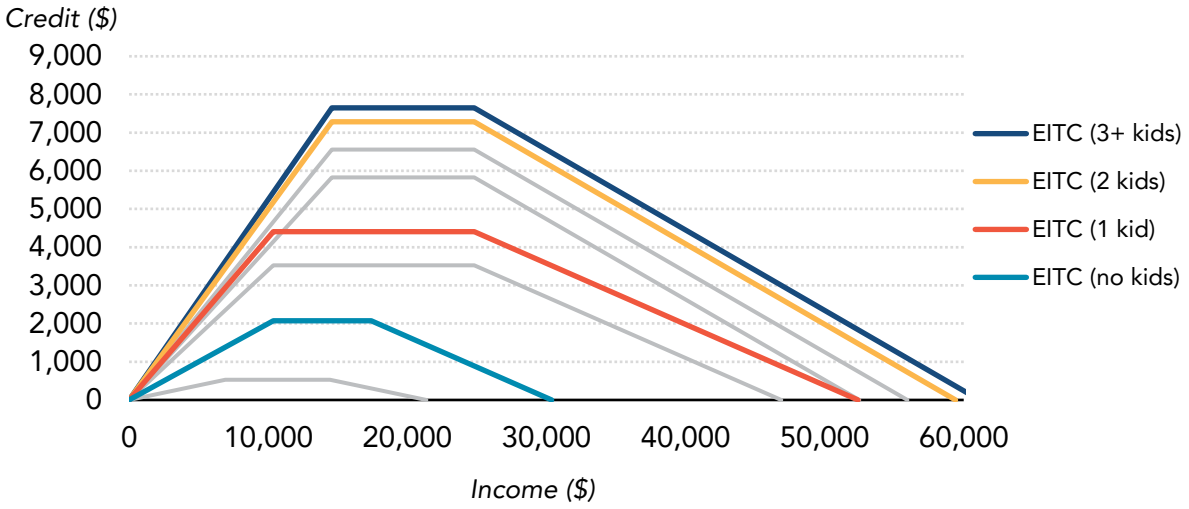
The WFTRA attempts to address income inequality and relatively poor outcomes for low-income children by increasing both the EITC and CTC. Roughly speaking, the WFTRA would increase the maximum EITC for families with children about 25 percent and quadruple the relatively small credit for workers without resident children. The bill also would significantly broaden the income range over which childless workers could receive a credit, meaning they would be treated much like workers with one child (figure 10 and table 1). Age limits for workers without children would be expanded from 25 to 64 under current law to 19 to 67 under the WFTRA.

The bill would allow families to receive the full $2,000 current-law CTC for each child under age 17 unless their income exceeded $200,000 (for married couples) or $150,000 (for single parents), at which point the credit would begin to phase out. Families with children under age 6 would also get an additional $1,000 young child tax credit. The CTC would be made fully refundable, meaning the entire credit would be paid to families regardless of whether they had income tax liability (figure 11 and table 2).

FIGURE 10

Working Families Tax Relief Act

Impact on EITC for married couples

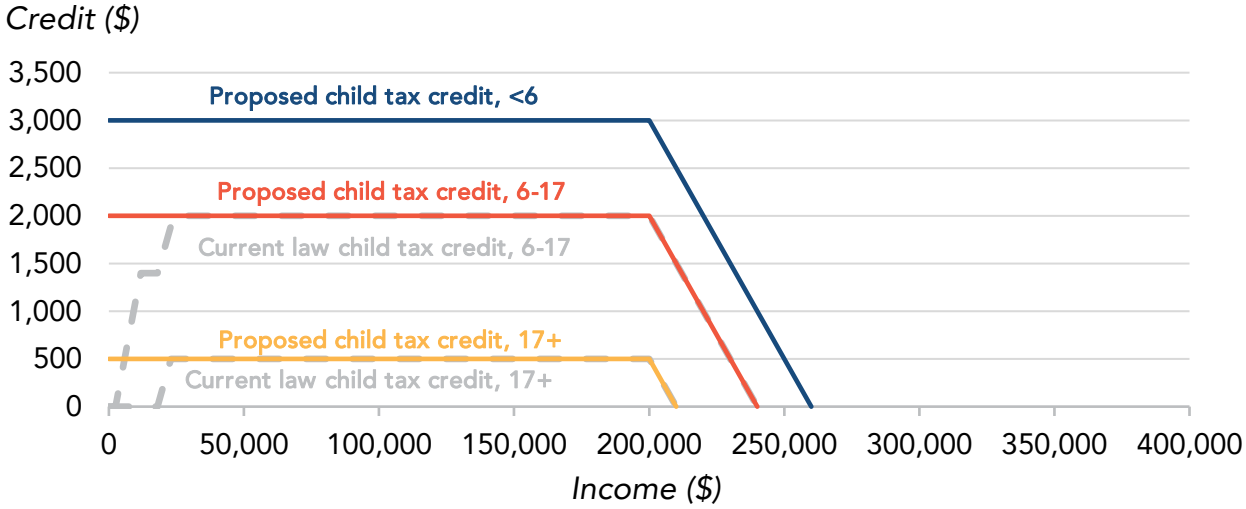


Source: Author's calculations
Note: Assumes all income comes from earnings. Gray lines are EITC for married couples under current law.

FIGURE 11

Child Tax Credit, Single Parent under WFTRA

One child, 2019



Source: Urban-Brookings Tax Policy Center calculations.
Note: Assumes all income comes from earnings, and child meets all tests to be a CTC-qualifying dependent. Credit for married parents begins to phase out at $400,000 of income. Only citizen children qualify for the $2,000 CTC for children under 17. Noncitizens under age 17 who meet the dependency tests of eligibility can qualify for the credit for other dependents.

TABLE 1

Basic Worker Credit Parameters

Current law and various proposals, 2019

	Credit rate (percent)	Minimum income for maximum credit	Maximum credit	Phaseout rate (percent)	Phaseout Range[a] Beginning income	Phaseout Range[a] Ending income
Current Law, Earned Income Tax Credit						
No children	7.65	6,920	529	7.65	8,650	15,570
One child	34	10,370	3,526	15.98	19,030	41,094
Two children	40	14,570	5,828	21.06	19,030	46,703
Three children	45	14,570	6,557	21.06	19,030	50,162
American Family Act (AFA)						
Would not change EITC in current law						
LIFT (Livable Incomes for Families Today) the Middle Class Act (S.4 Harris) [b]						
Single	100	3,000	3,000	15	30,000	50,000
Head of Household	100	3,000	3,000	15	60,000	80,000
Married	100	6,000	6,000	15	60,000	100,000
Cost-of-Living Refund (CRA) (S. 1849; H.R. 1431 (Brown, Khanna)[c]						
No children	30	10,370	3,111	15.98	19,030	15,270
One child	65.28	10,370	6,770	15.98	19,030	40,320
Two children	76.80	14,570	11,190	21.06	19,030	45,802
Three children	86.40	14,570	12,588	21.06	19,030	49,194
Working Families Tax Relief Act (WFTRA) (S. 1138 (Bennet, Brown, Durbin, Wyden)[c]						
No children	20	10,370	2,074	15.98	11,600	24,579
One child	42.5	10,370	4,407	15.98	19,030	46,608
Two children	50	14,570	7,285	21.06	19,030	53,622
Three children	52.5	14,570	7,649	21.06	19,030	55,349

Sources: Current law, 2019: Internal Revenue Service, Revenue Procedure 2018-57, downloaded August 5, 2019; Cost-of-Living Refund Act: H.R. 1431, 116th Congress and S. 527, 116th Congress; LIFT: S. 4, 116th Congress; WFTRA: S. 1138, 116th Congress.

Notes:

[a] The values of the beginning and ending points of the phase-out range are $5,800 higher in 2019 for no children and $5,790 for families with children, except for the LIFT Act. Married parameters for LIFT differ substantially and are separately included in the table.

[b] Maximum benefit of $1,200 allowed for nondependents who either receive a Pell grant or have incomes less than 250 percent of the federal poverty level and for certain caregivers. Benefits of the LIFT Act do not vary based on the number of qualifying children in the tax unit and are in addition to current-law benefits. Pell grant considered earnings for purposes of credit calculation.

[c] The Cost-of-Living Refund Act and WFTRA would replace existing EITC parameters with the above parameters, while the LIFT Act would implement an independent credit in addition to the existing EITC.

TABLE 2

Child Tax Credit Parameters

Current law and various proposals, 2019

	Minimum earnings to qualify for credit	Does credit phase-in?	Maximum credit refund	Maximum credit per child	Phaseout rate (percent)	Phaseout range[a]	
						Beginning income	Ending income
Current Law							
Child under 17	$2,500	Yes; 15 percent rate	$1,400	2,000	5	200,000	240,000
LIFT (Livable Incomes for Families Today) the Middle Class Act[b]							
Would not change CTC in current law.							
Cost-of-Living Refund (CRA)[b]							
Would not change CTC in current law.							
American Family Act (AFA)							
Child under 6	$0	Full credit allowed to all with incomes under the beginning of the phase-out	$3,600	3,600	5	130,000	190,000
Child 6–16	$0		$3,000	3,000	5	130,000	190,000
Working Families Tax Relief Act (WFTRA)							
Child under 6	$0	Full credit allowed to all with incomes under the beginning of the phase-out	$3,000	3,000	5	200,000	260,000
Child 6–16	$0		$2,000	2,000	5	200,000	240,000

Source: Current law, 2019: IRS Publication 972, Child Tax Credit, 2018, and IRS Revenue Procedure 2018-57.
American Family Act: S. 690, 116th Congress and H.R. 1560, 116th Congress.
WFTRA: S. 1138, 116th Congress.

Notes:

[a] Phaseout range is for a family with one child. The credit phases out over a longer range for families with more children. The beginning of the phaseout range stays the same, but it takes longer to phase out.

[b] CLR and LIFT do not amend the existing CTC or add a new child credit; AFA and WFTRA would amend the existing CTC.

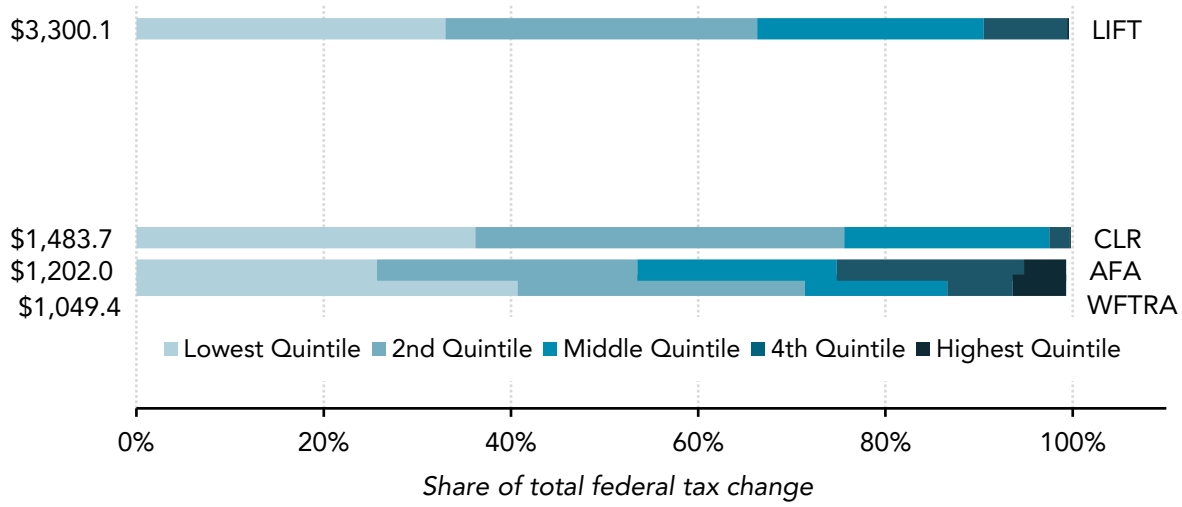
To compare the four proposals, we estimate the cost of each plan and how benefits from the plan would be distributed across income groups. We then analyze several variations of the plans, which allows us to consider how they might be altered by simple changes to their parameters.

How much the plans would reduce income inequality depends in part on how large the benefits are for low-income people relative to high-income people. Of course, this does not account for the tax base that finances the credits or the credit's effects on behavior. Still, distributing larger shares of the plan's benefits to lower income quintiles and smaller shares to higher income quintiles likely will reduce income inequality more than plans that distribute benefits more evenly. Already, higher-income families pay a larger share of federal income taxes than lower-income families (Congressional Budget Office 2019). These plans would likely cause higher-income families to pay an even greater share of that total tax burden.

FIGURE 12

Distribution of 2019 EITC and CTC Proposals
By share of net benefits distributed by income quintile

Proposal by estimated 10-year expenditures (billions)



Source: Tax Policy Center microsimulation model version 0718-1, T19-0027/0029 (LIFT), T19-0006/0008 (AFA), and preliminary estimates (CLR and WFTRA).
Note: Cost of proposals estimated over fiscal years 2019-2028. Income for quintiles is defined as expanded cash income.

In 2019, the WFTRA would deliver the largest share of total benefits to people in the lowest income quintile. Almost 42 percent of the proposal's total benefits would flow to this group (figure 12). An additional 30 percent of benefits would flow to units in the second income quintile. The proposal would deliver only a small share (5.6 percent) of total benefits to families in the highest income quintile. Total benefits distributed by the plan are the lowest of the four proposals (reducing revenues by $1.049 billion from fiscal years 2019 to 2028). Average benefits for the lowest income quintile (about $800) are high in 2019 relative to average benefits for the highest

income quintile (about $200; figure 13). We show the 2019 cost of the proposals in figure 13, which are ordered the same as the 10-year revenue cost of the proposals.

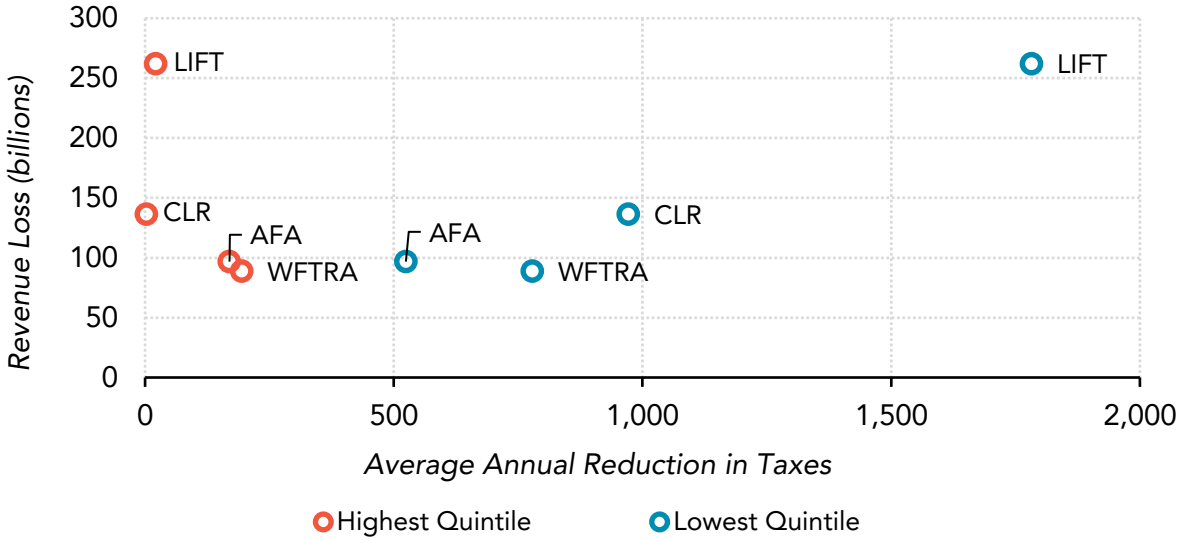
The CLR would provide about 36 percent of total plan benefits to families in the lowest income quintile and almost 40 percent of total benefits to families in the second income quintile. The CLR would provide less than 1 percent of benefits to families in the highest income quintile and less than 3 percent of total benefits to those in the top two income quintiles. The 10-year revenue cost of the CLR is higher than the WFTRA, and the difference between average benefits delivered to the lowest and highest income quintiles is larger as well. The CLR would provide, on average, about $1,000 a year to each family in the bottom income quintile and almost no benefit to the highest income quintile. As a result, the CLR does a better job reducing income inequality, but it does so at a higher revenue cost than the WFTRA.

The LIFT Act distributes about one-third of total benefits to families in each of the bottom two income quintiles and almost no benefit to families in the highest income quintile. The LIFT Act is the most expensive proposal we analyzed, and the difference in average benefits for the highest and lowest income quintiles is also the largest. The relatively large difference in average benefits between the highest and lowest income quintiles allows the LIFT Act to be most effective at reducing income inequality (at least by that measure) but at the highest revenue cost.

By design, the American Families Act (AFA) focuses on providing benefits to families with children rather than focusing more broadly on reducing income inequality. Across all families in the lowest income quintile, benefits average about $500, and benefits to families in the highest income quintile average about $200. As can often be the case with child-focused plans, the AFA provides almost one-quarter of benefits to families in the highest two income quintiles, though just under 5 percent of benefits would go to families in the highest income quintile. Child benefits, the focus of the AFA, tend to be distributed over a larger share of the population because children are present for families in all income categories. Despite having a revenue cost similar to the WFTRA, the AFA would be less effective at reducing overall income inequality.

FIGURE 13

Total Revenue Loss vs Tax Cut for Families in the Lowest and Highest Quintiles, 2019

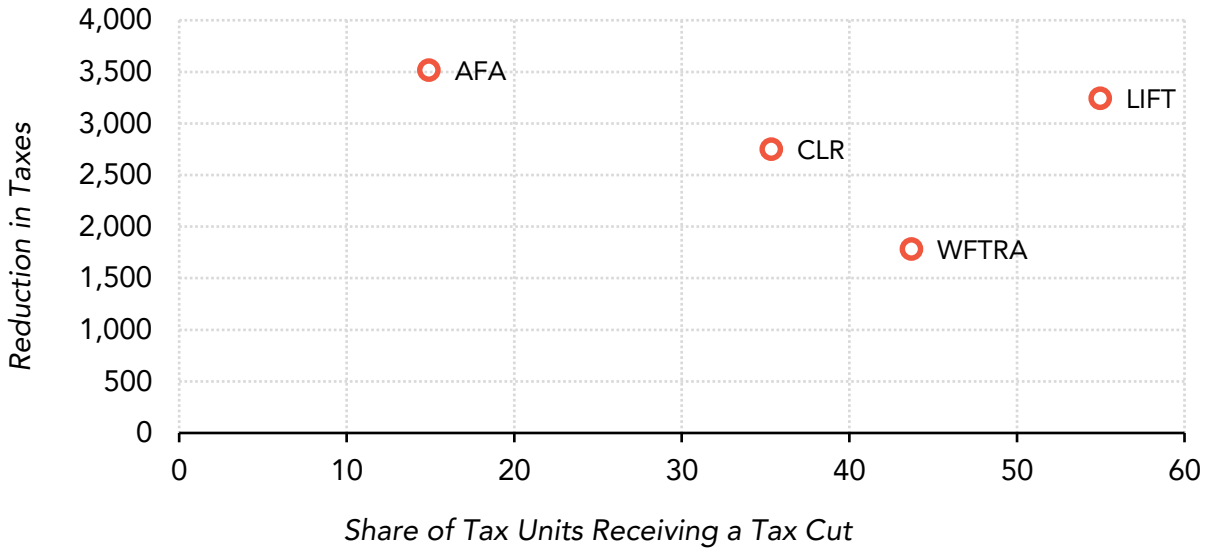


Source: Tax Policy Center microsimulation model version 0718-1.

Evaluating these proposals by the average change in taxes can be misleading because not all people in a given quintile would benefit. For example, the AFA would provide the largest benefit per family receiving benefits but would benefit the smallest number of families (figure 14). In contrast, the WFTRA would provide benefits to a larger share of families and a smaller average benefit to those families. The LIFT Act provides benefits to the largest share of families with an average benefit nearly as large as the AFA, and the two factors together lead to it having the highest revenue cost.

FIGURE 14

Share Receiving Tax Cut vs Reduction in Taxes for Families in the First Quintile

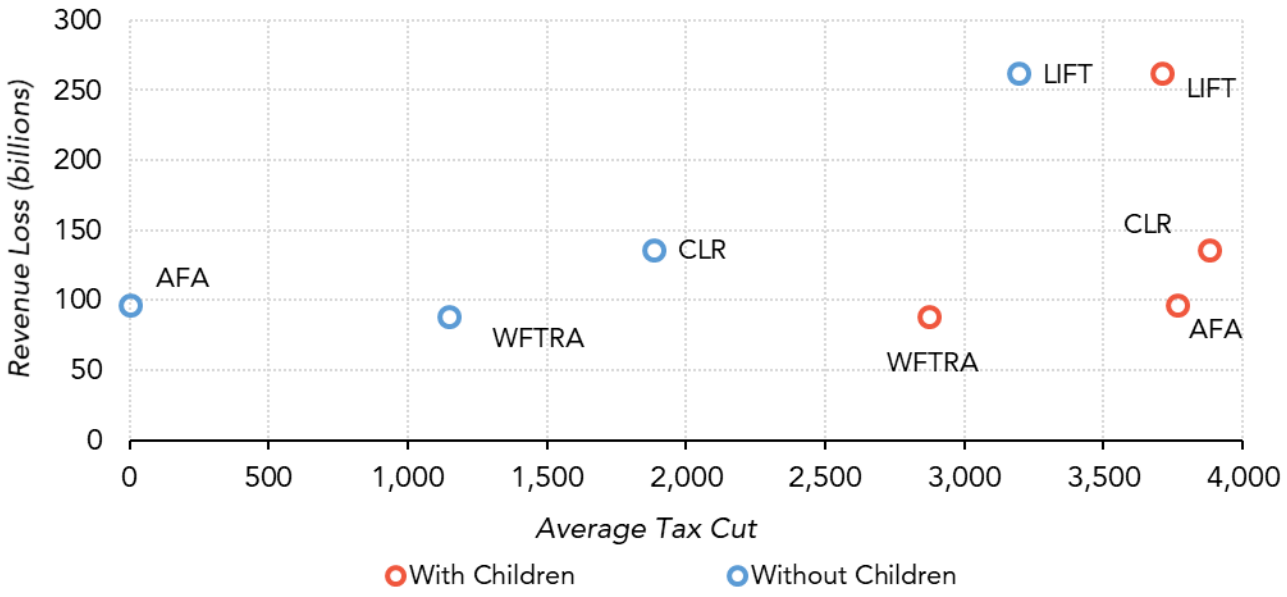


Source: Urban-Brookings Tax Policy Center Microsimulation Model version 0718-1.

Benefits to families in the first quintile can also can be broken down by families with and without children (figure 15). The AFA would provide almost no benefits to families without children, and the WFTRA and CLR provide very modest benefits, on average, to families without children. Although the LIFT Act bases benefits largely on marital status rather than the presence of children, families without children have much lower benefits, on average, because many in this group are elderly and do not qualify for benefits because they do not work. Families with children tend to be younger and are more likely to be working. Thus, the LIFT Act would provide the largest average benefit (relative to other plans analyzed) both for those with children and those without children, but it would do so at the largest revenue cost in 2019.

FIGURE 15

Total Revenue Loss vs Average Tax Cut For All Families With and Without Children



Source: Tax Policy Center microsimulation model version 0718-1

TRADE-OFFS AMONG PROPOSALS

Although each proposal helps low-income families and families with children in different ways, the exact elements of the provisions can seem somewhat arbitrary. For example, the AFA proposes to phase out the CTC starting at adjusted gross income of $180,000 for married couples filing jointly, but the sponsors could have chosen a phaseout beginning at $160,000. This lower phaseout would reduce the revenue loss without reducing the benefits received by families in the lowest income quintile with children (though it would reduce benefits for those higher-income families affected by the new phaseout range).

We evaluate several variations for each plan, emphasizing three features. First, increasing the CTC and EITC for any targeted set of taxpayers has a fiscal cost. Second, for any proposed plan, alternatives exist that cost no more to the federal government but can be more beneficial to target groups by being less beneficial to other groups. Third, for any proposed plan, alternatives exist that are less costly and are at least as beneficial to a target group but would be less beneficial to other groups. The appendix describes alternatives we tested.

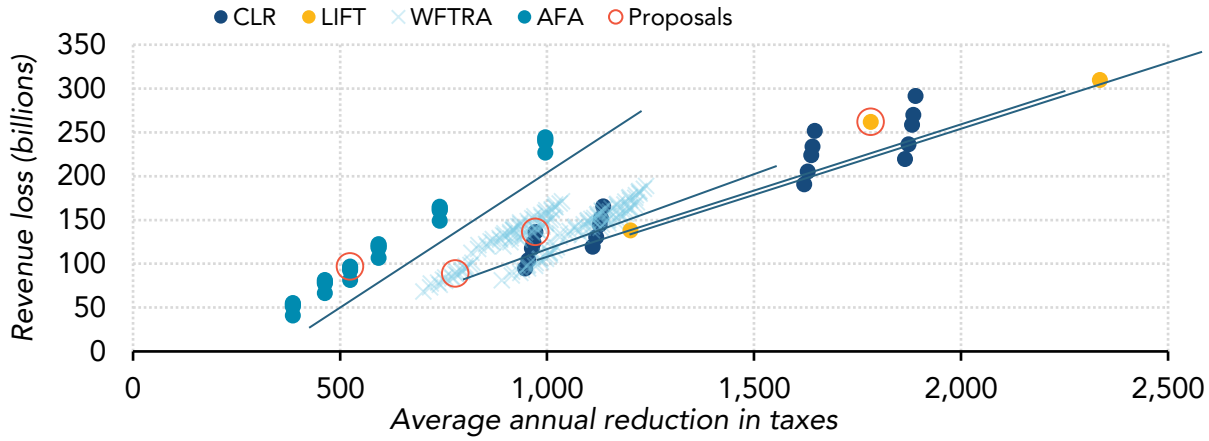
We considered changes to the various proposals by manipulating the following parameters:

- **WFTRA:** CTC credit amounts, EITC childless phase-in rates; EITC income level at which benefits phase out, and the phaseout rate
- **LIFT Act:** Maximum credit and phaseout rate to the new earnings subsidy
- **AFA:** Child credit phaseout rates and credit amounts
- **CLR:** EITC phase-in and phaseout rates

Here we focus on the consequences for two target groups: families in the lowest quintile of expanded cash income (our proxy for whether a plan addresses wage stagnation and economic inequality) and families with children (our proxy for whether a plan addresses the relatively poor outcomes for low-income children). Similar analyses can be conducted on other groups, such as families headed by someone at least 65 years old or with a different level of income.[vi]

FIGURE 16

Total Revenue Loss versus Tax Cuts for Households in the Lowest Quintile



Source: Urban-Brookings Tax Policy Center Microsimulation Model version 0718-1.
Note: AFA = the American Families Act; CLR = the cost-of-living refund; LIFT = the LIFT the Middle Class Act; WFTRA = the Working Families Tax Relief Act. Points represent variations on the proposals, with actual proposal circled in orange.

Considering reasonable alternatives reduces the stark differences in the original proposals (figure 14). For example, some variations of the WFTRA are similar to the CLR in their overall revenue cost and in the benefits provided to families in the lowest income quintile. Variations of the CLR can provide more benefits than the LIFT Act to families in the bottom quintile, although a variation of the LIFT Act surpasses other plans in both benefits provided to families in the lowest quintile and the overall loss of federal revenue.

Figure 16 uses trend lines to show that the relationship between the reduction of revenues and the benefits for families in the lowest income quintile (for the alternatives studied) in 2019 is generally linear. The AFA alternatives form a steeper line than the other policies because the AFA does not focus benefits only on low-income families but rather on all families with children. Under the AFA, providing an additional $100 of average annual benefits to families in the lowest quintile reduces federal revenue by about $31 billion in 2019 because the structure of the act would provide similar benefits to many families in other parts of the income distribution. In comparison, an additional $100 of benefits to this same group of families in the lowest income quintile under the CLR or LIFT costs about $15 billion in 2019, and $100 of average annual benefits to those families under the WFTRA reduces revenues about $17 billion in 2019.

Each proposal also provides opportunities to either reduce the fiscal cost with no reduction in benefits to families in the lowest income quintile or increase benefits to this group of families at the same revenue cost. In figure 16, these appear as alternatives below and to the right of a given proposal. We demonstrate with two alternative plans.

In the first, we find a plan that provides at least as much in benefits to families in the lowest income quintile as the CLR but at a lower overall revenue cost. These are represented in figure 16 by values below and to the right of the original CLR proposal. As shown in table 3 alternative 1, a variation of WFTRA exists that would cost about $35 billion less per year than the CLR: the CLR would lose $136.1 billion in 2019 while the WFTRA alternative would only lose $101.1 billion in that year. But the benefits provided to families in the lowest income quintile would be the same at about $972. These savings are achieved by adjusting the WFTRA so that the childless EITC phases in at 30 percent per dollar of adjusted gross income rather than the proposed 20 percent (see table A.4). Moreover, the overall EITC phases out 10 percent faster. This combination of faster phase-in for the childless EITC and faster phaseout for the overall EITC effectively concentrates the total benefits to lower-income families while raising average benefits to the recipients. This allows the costs to decline without lowering benefits to families in the bottom quintile.

In the second variation, we find a plan that provides more benefits than the LIFT Act to families in the lowest income quintile but at no higher cost in forgone revenue. Here, a variation of the CLR is made more generous to families in the lowest quintile by phasing in its EITC twice as quickly and applying a 50 percent higher phaseout rate (table A.2). Consequently, this variation costs about the same amount in 2019 as the LIFT Act but provides an additional $100 in average annual benefits to families in the lowest income quintile (alternative 1 in table 4).

Of course, if these alternatives either cost less or the same as another plan and provide more benefits to families in the lowest quintile, other groups must receive lower benefits than the original proposal provides. Thus, in the first comparison, families in the second and third quintile receive fewer benefits under the WFTRA

alternative than under the CLR proposal. In the second comparison, families in the third and fourth quintile receive fewer benefits under the CLR alternative than under the LIFT proposal.

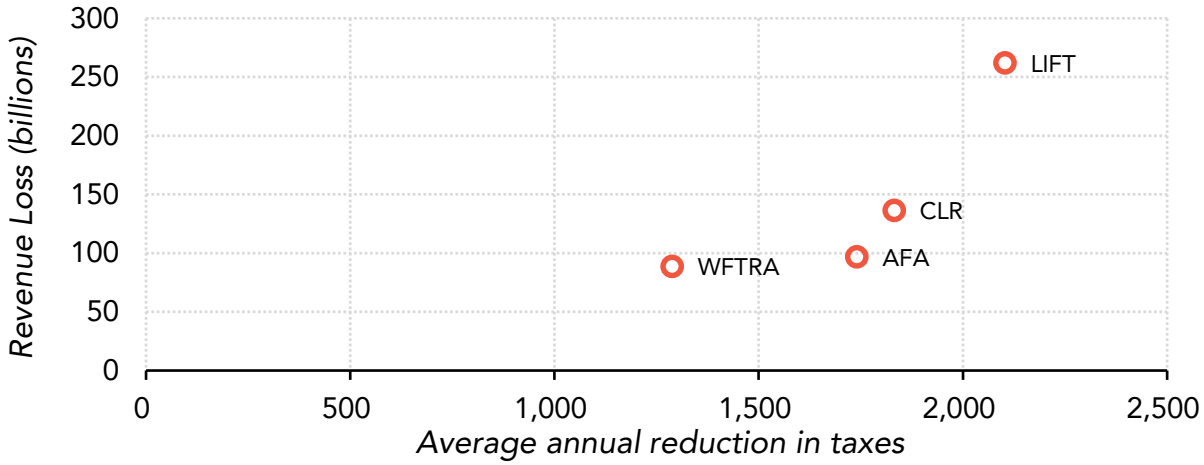
Further, even within the lowest income quintile, each comparison creates winners and losers among families. In the first comparison, the WFTRA alternative provides more benefits to married couples in the lowest quintile who file their taxes jointly, but it would provide smaller average benefits to taxpayers filing as heads of household (single parents). In the second comparison, taxpayers in the lowest quintile who file as heads of household receive larger average benefits from the CLR alternative. Married couples in the lowest income quintile filing jointly would receive relatively smaller benefits even if they claim dependent children.

Families with children, regardless of income, form our second focus. We plot the LIFT Act, the CLR, the WFTRA, and the AFA in terms of (a) their average effects on those families with children across all incomes and (b) the loss of revenue for 2019 (figure 17). The WFTRA would be the least costly, reducing federal revenues by about $88 billion in 2019. As one consequence, however, it would provide the smallest average annual benefit to families with children (an average of about $1,300). The LIFT Act, on the other hand, would reduce federal revenues by about $262 billion in 2019 while cutting annual taxes to units in the first income quintile by more than $2,100 on average. The CLR lies approximately between these two, while the AFA lies substantially to the right of WFTRA. This shows that the AFA, although costing slightly more than WFTRA, provides much larger benefits to families with children.

These proposals could be modified to more closely resemble each other. For instance, by raising the credit level for families with children under age 6, the WFTRA could be modified so that the average family in the lowest income quintile with children receives closer to $3,500 and $4,000 in benefits. Its overall revenue cost would then increase unless it also reduced benefits to families at higher income levels. Alternatively, the LIFT Act could be made less costly by covering fewer workers.

FIGURE 17

Total Revenue Loss vs Average Tax Cut for All Families with Children



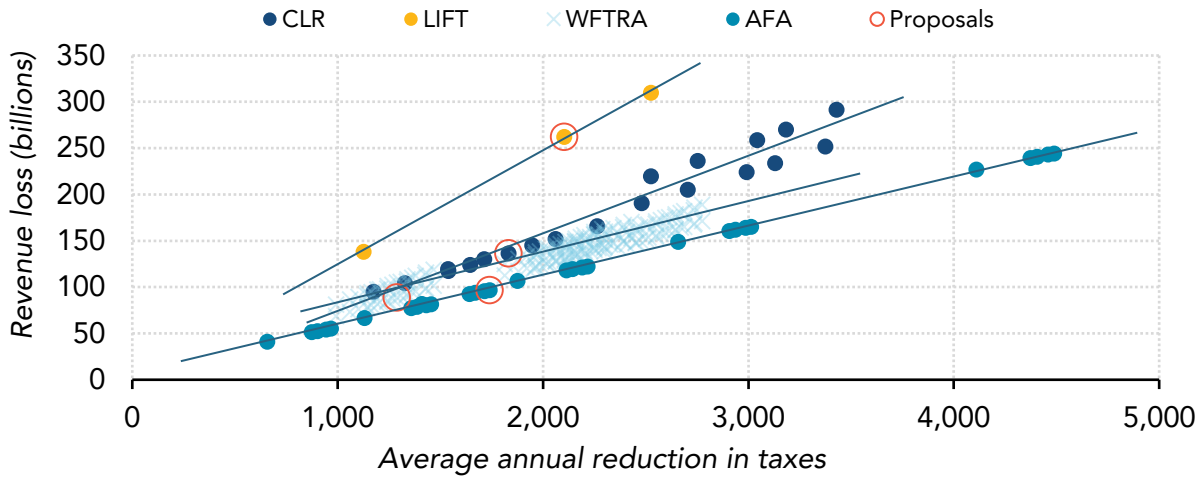
Source: Urban-Brookings Tax Policy Center microsimulation model version 0718-1.
Notes: AFA = the American Families Act; CTC = the child tax credit; CLR = the cost-of-living refund; EITC = the earned income tax credit; LIFT = the LIFT the Middle Class Act; WFTRA = the Working Families Tax Relief Act.

This holds as well for the alternatives we consider (figure 18). Because the AFA focuses exclusively on families with children, its variations are the least expensive method for providing any total level of benefits for those families. So even though the WFTRA, as proposed, is the least costly, some variations of the AFA would cost still less while providing larger benefits to families with children.

Because the LIFT Act would provide benefits to families both with and without children, and in roughly equal measure, it is the most expensive per dollar reduction in taxes for families with children and consequently the most expensive approach to increase benefits for these families. The steeper slope of the LIFT Act's trend line reflects this. For variations on the LIFT Act, each additional $100 in average annual benefits for families with children costs an additional $12.4 billion a year. For the AFA, an additional $100 in average annual benefits for families with children reduces federal revenue by about $5.4 billion a year. Several variations of the CLR and WFTRA are available, but across all options, an extra $100 in average annual benefits to families with children from the CLR reduces federal revenues by about $8.4 billion a year, and an extra $100 in average annual benefits to these same families from the WFTRA reduces federal revenues by about $5.5 billion a year.

FIGURE 18

Total Revenue Loss vs Average Tax Cut for All Families with Children



Source: Urban-Brookings Tax Policy Center Microsimulation Model version 0718-1.
Note: AFA = the American Families Act; CLR = the cost-of-living refund; LIFT = the LIFT the Middle Class Act; WFTRA = the Working Families Tax Relief Act. Points represent variations on proposed credits, with actual proposals circled in orange.

As before, there are alternatives for each proposal that would either provide greater benefits to the target group (families with children) or provide the same level of benefits to the target group at a lower overall revenue cost. In table 3, we present a sample plan that provides the largest average annual benefits to families with children while costing no more than the CLR. Alternative 2 is a variation of the AFA that would reduce revenue less than the CLR but provide $1,875 of benefits, on average, to families with children. Under this alternative, the CTC would start to phase out at only $120,000 of adjusted gross income for those filing jointly, but the maximum credit amount would increase to $3,600 (table A.1).

In table 5, we provide an estimate for a sample plan that costs no more than LIFT in forgone revenue but would provide larger average benefits to families with children. This alternative version of the AFA would more than double the average annual tax benefit among families with children (from $2,104 to $4,488) at nearly the same annual revenue cost ($262.0 billion versus $265.0 billion). Under this alternative, the CTC would be raised to $4,000, while benefits would phase out as in the proposed AFA (table A.1).

As before, alternatives that either cost less in forgone revenue or provide larger annual benefits to families with children must provide smaller benefits to other groups. Compared with the CLR, the AFA alternative in table 3 would provide smaller benefits to single parents. Among those families with child dependents, the AFA

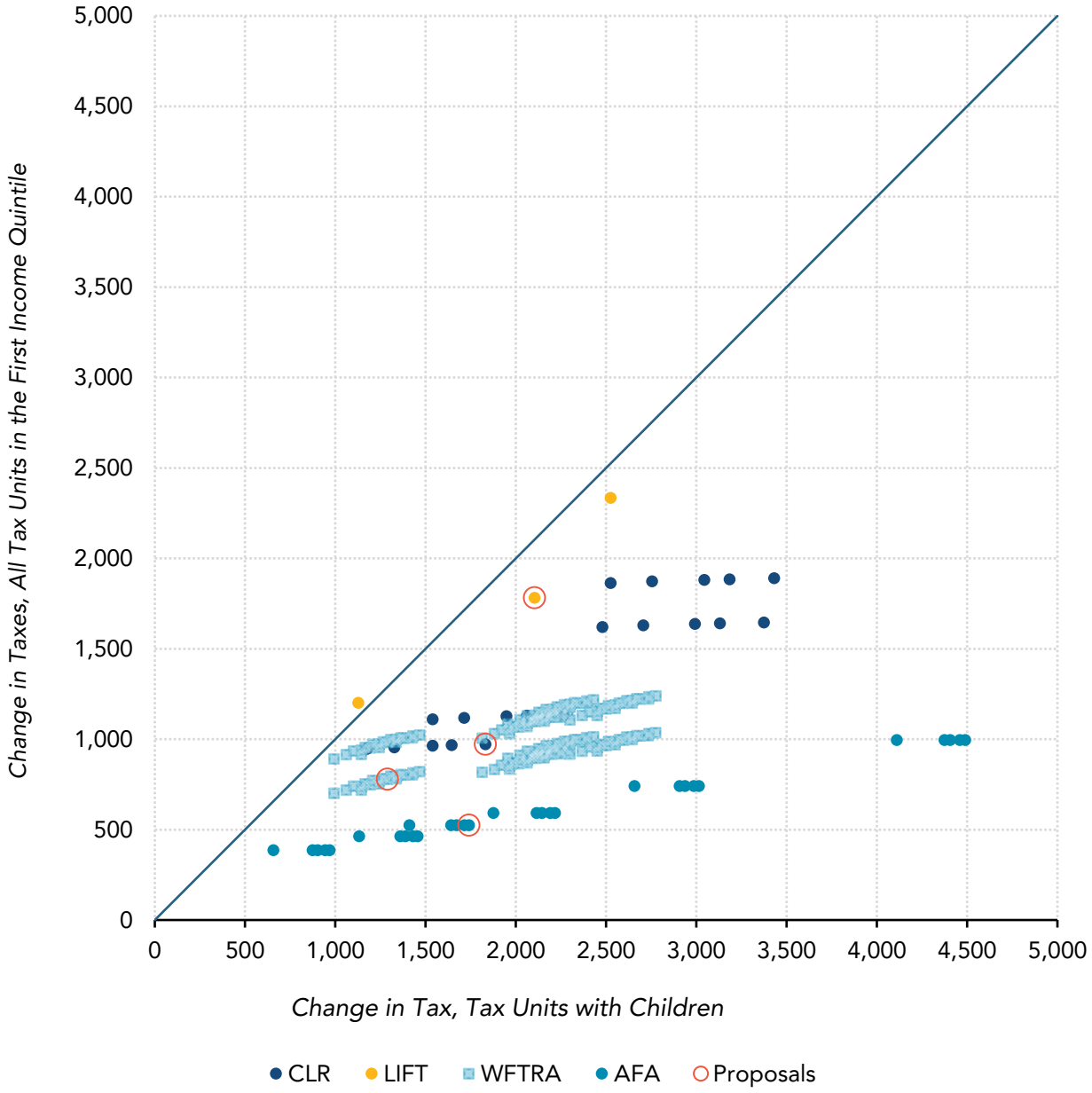
alternative would provide larger benefits to families in the lowest, third, and fourth income quintiles but smaller benefits to families in the second and fifth quintiles. Compared with the LIFT Act, the AFA alternative in table 4 would provide much smaller benefits to those families without children. However, it also provides larger average benefits to families with children in all five quintiles.

Finally, to emphasize the trade-offs between families in the lowest quintile and families with children, in figure 19 we plot the results for one group against the other. Each point represents the change in taxes for two different populations: families with children on the horizontal axis and families in the bottom income quintile on the vertical axis. Along the 45-degree line, the two groups receive similar tax cuts. Plans toward the upper right provide more and larger tax cuts to both groups; plans on the bottom left provide smaller tax cuts to both groups. Plans to the right of the 45-degree line provide larger tax cuts to families with children; plans to the left provide larger tax cuts to families in the bottom income quintile.

One variation of the LIFT Act lies to the left of the 45-degree line, indicating that it would provide about the same benefits to families with children and families in the bottom income quintile. All other plans, including the proposals, would be more beneficial to families with children than to families in the lowest income quintile.

FIGURE 19

Change in Taxes for Families with Children versus Families in the Lowest Income Quintile



Source: Urban-Brookings Tax Policy Center microsimulation model 0718-1.

TABLE 3

Plans That Benefit Families in the Lowest Quintile at Least as Much as the CLR but Cost Less

2019

Proposal	Alternative	Revenue Loss	Average Reduction in Taxes	
			Families with Children	Families in the First Income Quintile
CLR		136.2 billion	1,832	971
WFTRA	Alternative 1	101.1 billion	-	972
AFA	Alternative 2	106.8 billion	1,875	-

Source: Tax Policy Center Microsimulation Model version 0718-1

TABLE 4

Plans That Cost No More than LIFT with Greater Benefits to Families with Children.

2019

Proposal	Alternative	Revenue Loss	Average Reduction in Taxes	
			Families with Children	Families in the First Income Quintile
LIFT		265.5 billion	2,104	1,782
CLR	Alternative 1	258.4 billion	-	1,882
AFA	Alternative 2	262.0 billion	4,488	-

Source: Tax Policy Center Microsimulation Model version 0718-1

Policymakers have proposed several large-scale earnings and child subsidy expansions that build on the EITC and CTC. The four proposals examined here satisfy several goals, such as reducing income inequality, improving outcomes for children, and covering some low-earning workers now mainly excluded from wage subsidies. In practice, all grant the largest additional benefits to families with children. By focusing on low-income workers, two proposals add modestly to benefits for childless workers, and one adds substantially both to those workers and to low earners who marry other low earners. But policies that aim only to subsidize work regardless of whether children are present still tend to greatly benefit families with children because working families on average are more likely to be caring for children than retired and other nonworking families.

All else equal, proposals that build on the existing CTC (which is nearly universal among families with children) tend to have higher costs and be less progressive than those built on the EITC because the former apply to more families, including many middle-class families. On the other hand, raising benefits for both families with children and workers largely left out of the existing EITC and CTC can easily cost more than raising benefits for only one of those groups. Focusing only on childless workers can be relatively modest in cost and provide large benefits to this group. If benefits for low-income families are increased by setting the phaseout income levels greater than under current law, benefits can extend beyond the lowest income quintile and raise overall revenue costs. Increasing benefits to one group without raising costs necessarily entails lowering benefits for other groups.

Trade-offs are not easy or avoidable. Legislators must ultimately decide which needs in society are most pressing and which policies, including the taxes or benefit cuts required to pay for those policies, address those needs most fairly and efficiently. This report lays out some of those trade-offs by looking at the costs and distributional effects of four existing proposals and variations on these proposals.

TABLE A1

American Family Act

Parameters and alternatives

CTC Phase-out Options		CTC Credit Amounts	
Married Filing Jointly	Other	Married Filing Jointly	Other
180,000	**130,000**	**3,000**	**3,600**
180,000	90,000	3,000	3,000
160,000	110,000	3,600	3,600
160,000	80,000	2,500	2,800
120,000	60,000	4,000	4,600
		5,000	6,000

Note: Values used in the original proposal marked in bold.

TABLE A2

Cost-of-Living Refund Act

Parameters and alternatives

	EITC Phase-in Rate (% increase per dollar AGI)				EITC Phase-out rate (% decrease per dollar AGI)		
Description	Childless	1 child	2 child	3+ child	Description	0 or 1 child	2+ children
Proposal	**30**	**65.3**	**76.8**	**86.4**	**Proposal**	**16.0**	**21.1**
10 Percent faster	33	71.8	84.5	95.0	30 Percent Faster	20.8	27.4
50 Percent faster*	45	97.9	100.0	100.0	50 Percent Faster	24.0	31.6
Twice as fast*	60	100.0	100.0	100.0	Twice as fast	32.0	42.1
					Two and half times as fast	40.0	52.7

Note: Values used in the original proposal marked in bold; * Phase-in rate cannot exceed 100 percent.

TABLE A2

Cost-of-Living Refund (Gain) Act

Parameters and alternatives

EITC Phase-in Rate				EITC Phase-out rate			
Childless	1 child	2 child	3+ child	Childless	1 child	2 child	3+ child
0.3	**0.6528**	**0.768**	**0.864**	**0.1598**	**0.1598**	**0.2106**	**0.2106**
0.33	0.71808	0.8448	0.9504	0.20774	0.20774	0.27378	0.27378
0.45	0.9792	1	1	0.2397	0.2397	0.3159	0.3159
0.6	1	1	1	0.3196	0.3196	0.4212	0.4212
				0.3995	0.3995	0.5265	0.5265

Note: Values used in the original proposal marked in bold

TABLE A3

LIFT (Livable Incomes for Families Today) the Middle Class Act

Parameters and alternatives

Phase-in endpoint, maximum credit			Phase-out range		
Single	Head of Household	Married Filing Jointly	Single	Head of Household	Married Filing Jointly
3,000	**3,000**	**6,000**	**30,000-50,000**	**80,000-100,000**	**60,000-100,000**
2,000	2,000	4,000	20,000-40,000	60,000-80,000	40,000-80,000
4,000	4,000	8,000	25,000-45,000	70,000-90,000	50,000-90,000

Note: Values used in the original proposal marked in bold.

TABLE A4

Working Families Tax Relief Act

Parameters and alternatives

	CTC Credit Amounts		EITC Childless Phase-in rate (% decrease per dollar AGI)
	Child 6+	Child under 6	
	2,000	**3,000**	**20%**
	3,000	3,000	30%
	3,000	4,000	
	2,000	5,000	

	Location of second EITC Kink Point				EITC Phase-out rate (% decrease per dollar AGI)		
Description	Childless	1 child	2 child	3+ child	Description	0 or 1 child	2+ children
Proposal	**11,610**	**19,040**	**19,040**	**19,040**	**Proposal**	**16.0**	**21.1**
10 percent lower	10,449	17,136	17,136	17,136	Same as proposal for 2+ children	21.1	21.1
10 percent higher	12,771	20,944	20,944	20,944	10 percent faster	17.6	23.2
20 percent higher	13,932	22,848	22,848	22,848	30 percent faster	20.8	27.4
					50 percent faster	24.0	31.6

Note: Values used in the original proposal marked in bold.

NOTES

[i] All analysis is based on tax units, including nonfiling tax units. For ease of exposition, we use the term "family."

[ii] Some workers who are "childless" for tax purposes have noncustodial children, children over age 19 and not in postsecondary school full-time in at least five months of the year, or over age 24.

[iii] See also Dyaln Matthews, "Paul Ryan's Poverty Plan," *Vox*, July 24, 2014, https://www.vox.com/2014/7/24/18080430/paul-ryan-poverty.

[iv] The TCJA adopted a new measure of inflation that applies to much of the federal income tax code, including the EITC. The maximum EITC will now grow at a slower rate of inflation each year. For more information, see Tax Policy Center Table T17-0312, "Conference Agreement: The Tax Cuts and Jobs Act; Baseline Current Law; Distribution of Federal Tax Change by Expanded Cash Income Percentile, 2018," accessed October 17, 2019.

[v] Tax Policy Center Table T19-0025, "Tax Benefit of the Earned Income Tax Credit, Baseline: Current Law, Distribution of Federal Tax Change by Expanded Cash Income Level, 2019," accessed October 21, 2019.

[vi] Policymakers frequently measure the benefits of a proposal in terms of the change in taxes, so all of our analyses are presented in terms of total or average tax changes. Many economists, on the other hand, focus on changes in after-tax income. See Gale (2017) for more information.

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