TAX POLICY CENTER
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EXTENDING THE CALIFORNIA EARNED INCOME TAX CREDIT TO POSTSECONDARY STUDENTS

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Postsecondary education can be a critical step toward financial independence. But analysis of total college costs in California has shown that for many people with low incomes, college may present an extraordinary financial burden. For students with incomes under $30,000 in California, the cost of attendance at public universities (after accounting for existing grant aid) consumes about half of a person's household income. This is less than the national average but is still substantial (TICAS 2017).

One way to provide additional assistance to students who struggle would be to extend the maximum California earned income tax credit (CalEITC) to students who are independent for tax purposes, including students with no earnings, even if they did not work enough to qualify for the maximum credit. This would essentially mean that for these students, the tax code treats going to school the same as working. Students who are independent for tax purposes tend to be particularly disadvantaged: they include non-traditional-age students (those age 24 and older) who often have responsibilities outside of school or may be married and have children; they also include traditional-age students who are no longer supported by parents or other relatives. For example, students who are in foster care, have aged out of foster care, or were adopted out of foster care after reaching age 13 are automatically considered independent for purposes of calculating student aid and are likely to be independent for tax purposes as well.

We estimate that about two-thirds of independent students in California already benefit from the state's EITC. Focusing on independent students with incomes under $30,000, 87 percent receive a benefit. Under the proposal, 6 percent of independent students with income below $30,000 would receive larger EITCs than under current law, and 8 percent of students with income below $30,000 would be newly eligible for benefits. All of the students who would receive higher benefits or become newly eligible for benefits have very low incomes. The proposal would deliver $46 million in additional benefits each year to 146,000 students (11 percent of all independent students). Almost all students who would benefit from the proposal do not have dependent children at home, so the proposal would allow them to be eligible for the maximum CalEITC for childless taxpayers.

The average increase in CalEITC benefits among independent students who would benefit from the proposal would be $312. On average, students with no children at home who would benefit from the proposal would receive a credit increase of about $180, and students with children at home who would benefit from the proposal would receive an average credit boost of about $1,200. This reflects the design of the CalEITC, which provides a maximum credit of up to $240 for people without children living at home and almost $3,000 for students with at least three children at home. This is similar to the federal EITC, which provides childless beneficiaries with a much smaller maximum benefit and which is available only to those with fairly low incomes. The proposal represents another step in California's continuous efforts to expand the state's EITC to include additional groups of people in need of assistance.

This policy brief describes how the CalEITC works, why independent students in California need financial assistance, why extending the CalEITC provides a relatively simple source of additional student aid, and the benefits of extending the maximum credit to students who are independent for tax purposes.

HOW DOES THE CALIFORNIA EITC WORK?

Under current law, workers receive a credit equal to a percentage of their earnings, up to a maximum credit. Both the credit rate and the maximum credit vary by family size, with larger credits available to families with more children. After the credit reaches its maximum, it declines with each additional dollar of income until no credit is available (figure 1). The CalEITC phases out sharply at first and then more slowly, a design intended to make sure families with incomes up to $30,000 receive at least some benefit. The CalEITC is a refundable tax credit, meaning the credit first offsets taxes owed and any additional credit a person qualifies for is delivered as a tax refund after filing a tax return.[1]

As with the federal EITC, no minimum age of eligibility applies to families with children. A person without children at home must be at least age 18 to benefit from the CalEITC. This is lower than the federal age limit of 25, so there are some people who receive the CalEITC even though they are ineligible for the federal EITC, including independent students ages 18 to 24 who are working for pay.

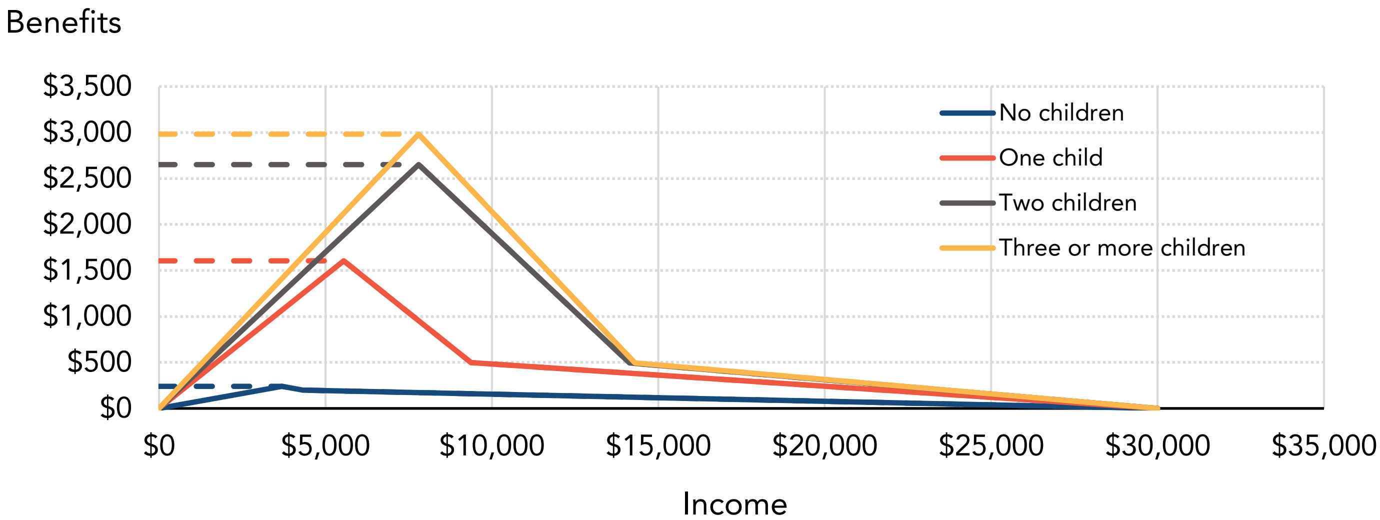
By design, the CalEITC only benefits people who work for pay. This can cause postsecondary students to be fully or partially excluded either because they do not work for pay or because they do not work enough to qualify for the maximum credit. In recognition of the importance of postsecondary education, including to retrain for new careers, the Economic Security Project has proposed extending the maximum credit benefit to low-income, independent students who attend school at least half time.[2]

[1] For additional information on the design, implementation, and subsequent expansions of the California EITC, see for example Rothstein and Montialoux (2015), Thorman and Danielson (2018), Anderson and Kimberlin (2019), and Petek (2019).

[2] For an analysis of an expansion of the federal EITC and how students would be affected, see Maag, Airi, Baum, and Rueben (2020).

FIGURE 1

California EITC (CalEITC), 2020



Source: Urban-Brookings Tax Policy Center
Note: Proposed expansion for low-income students independent for tax and aid purposes in dotted lines. Assumes all income comes from earnings. Reflects credit for tax year 2019.

The Proposal

We analyze what would happen if the maximum California EITC were made available to low-income postsecondary students who are independent for tax purposes (figure 1, dashed lines). This follows a more expansive proposal to expand the maximum federal EITC and expand it to students (Maag, Marron, and Huffer 2019; Maag et al. 2020).

Since establishing the CalEITC in 2015, the state government has expanded the credit several times to reach low-income workers left out from receiving benefits. This included an expansion to allow self-employment income to count toward credit calculation (originally it was excluded); a reduction of the age limit from 25 to 18 to include younger, childless workers; and an expansion to include undocumented workers. Each of these broadened the group of people eligible for the credit, just as extending the maximum credit to independent postsecondary students would do.

STUDENTS IN CALIFORNIA NEED ADDITIONAL ASSISTANCE

Students who are independent for tax purposes tend to be particularly disadvantaged. Independent students often cannot rely on assistance or aid from extended family to complete their education. Public and institutional financial aid is critical for college access in California, where 60 percent of public K–12 students qualify for free or reduced-price lunches (Johnson 2014).

Many students with children (20 percent of all California students) have significant needs when it comes to financing their college educations. Half of students with children in California rely on financial aid or excessive work to pay for their education (Walsh and Granville 2020).

Many (but not all) of these students with needs will qualify for traditional federal student aid, such as subsidized loans, Pell grants, or state aid such as the Cal Grant, but these programs often fall short of covering all student need, especially when considered over the entire period needed to complete a degree or certificate program. Moreover, the

Cal Grant—a grant designed to assist low-income students in California—is not an entitlement, so some people who qualify for benefits will not receive them (Cochrane 2019; Walsh and Granville 2020).

Advantages of Expanding the California EITC

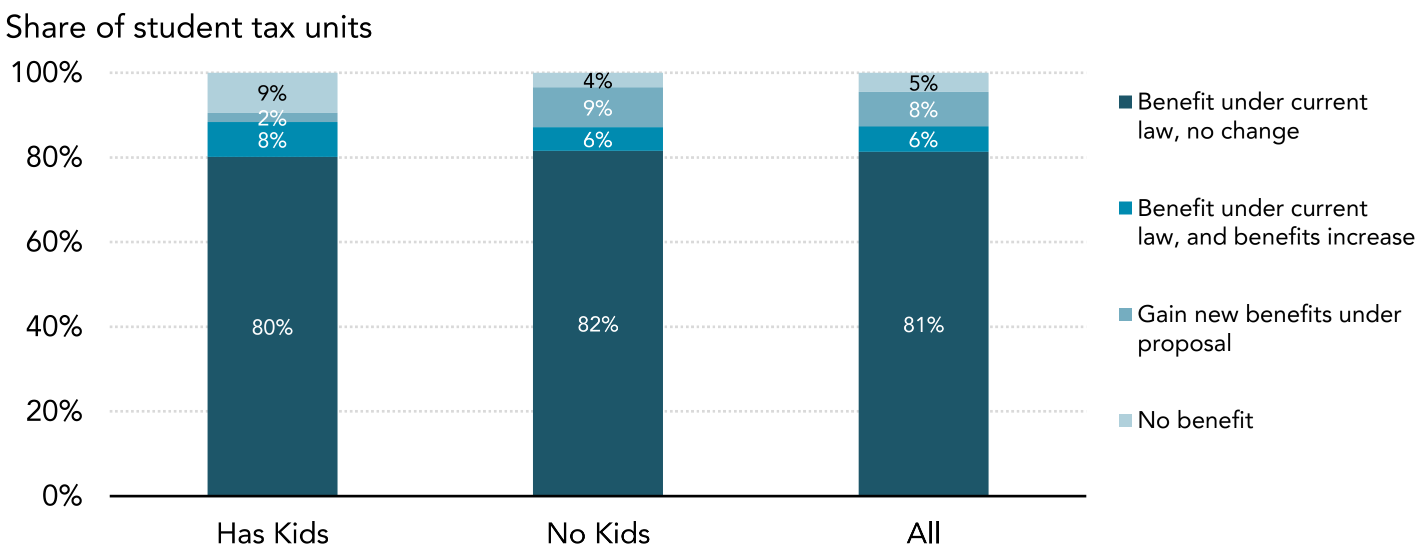
Extending the maximum CalEITC to independent students has several advantages over increasing traditional aid. State policy changes can often be implemented more quickly than a redesign of the federal aid programs (including the largest source of aid for low-income students, the Pell grant). Expanding the CalEITC would provide a demonstration of how the federal EITC could also be expanded. The CalEITC would provide flexible cash and avoid unnecessary complexity, allowing people to use the money for their most pressing needs (needs that may not be directly related to school but could help a student stay in school). Benefits from the CalEITC do not run the risk of overlapping (and thus reducing) aid from other sources, such as scholarships or the American Opportunity Tax Credit, that can only be used for a dedicated purpose (e.g., tuition and fees). The CalEITC is not taxable, unlike some grant aid. If grant aid is used for an expense other than a "qualified education expense" (typically tuition, fees, books and other course-related expenses), it becomes taxable at the state and federal level. Unlike loans, the credit does not need to be paid back.

ANALYSIS

Extending the maximum benefit of the CalEITC to low-income independent students would deliver $46 million in benefits, almost all (96 percent) to students with adjusted gross income less than $10,000. We estimate 15 percent of independent students with adjusted gross income less than $30,000 would benefit from expanding the CalEITC (figure 2). As a result of this expansion, the share of low-income students with EITC benefits would increase from 87 percent to 95 percent. A small share of students who already receive EITC benefits under current law would also get a larger credit.

FIGURE 2

Share of Students with Income Below $30,000 Benefiting from California EITC (CalEITC) Expansion



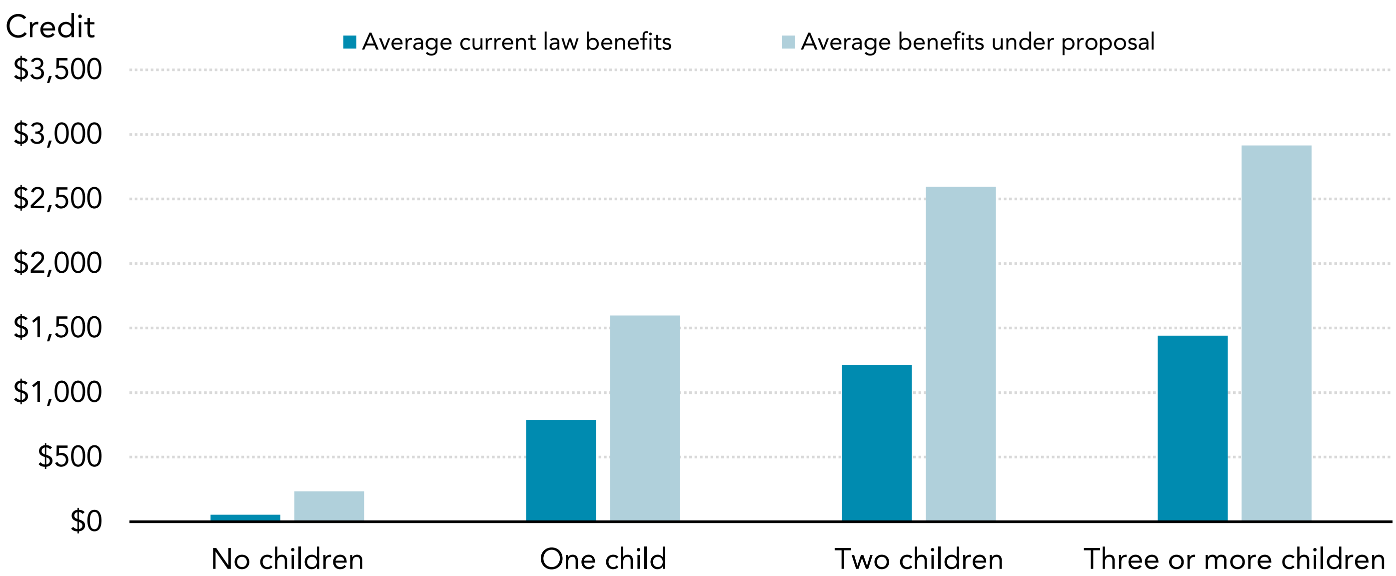
Source: Tax Policy Center State Income Tax Model, authors' calculations.
Note: Shows students with $0 to $30,000 in adjusted gross income.

The CalEITC is designed to deliver larger benefits to parents with children living at home than to people without children living at home, and the same would be true of students who were made newly eligible for benefits. Among all independent students who would benefit from the proposal, average benefits would rise by $183 for students with no children at home. The average increase in credit benefits for students who would benefit from the proposal with children at home would be $810 for those with one child, $1,380 for those with two children, and $1,470 for those with three or more children (figure 3). Almost all beneficiaries would be students with no children at home. Students not working for pay would see the starkest change: they would go from being ineligible for the credit to being eligible for the maximum credit (up to $3,000 for a student with three children at home).

FIGURE 3

Average EITC Benefits Under Current Law and Proposal

Independent students who benefit from the proposal



Source: Tax Policy Center State Income Tax Model.

CONCLUSION

California has a robust student aid system, but students with incomes under $30,000 often must spend half their incomes to attend public universities, even after accounting for grant aid. One way to provide additional aid to independent students in California, who may be particularly disadvantaged, would be to extend the maximum benefit from the CalEITC to those whose earnings are too low for them to qualify for the maximum credit. This would continue a series of changes to the CalEITC intended to increase the credit's coverage of disadvantaged groups.

Extending the maximum CalEITC to independent students would deliver about $46 million in benefits to 146,000 California taxpayers. The average increase in benefits for independent students without children at home would be about $180. Students with children at home would receive an average increase in benefits of about $1,200, with higher average benefits going to those with more children.

Extending the CalEITC to students would provide a new source of flexible cash that would not risk interfering with existing grant and scholarship aid. Students could use the money to best meet their needs.

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