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Earnings Requirements, Benefit Values, and Child Poverty under the Child Tax Credit:

Eliminating the earnings requirement does more to impact child poverty than increasing benefit levels

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The Child Tax Credit (CTC) is the largest child-related benefit received by families and children in the United States. Under the latest expansion of the CTC through the Tax Cuts and Jobs Act (TCJA), families can receive up to $2,000 per child, and there is currently support behind efforts to increase the maximum credit value. But, as this brief demonstrates, even if the maximum credit value were to increase, families below the poverty line would only see a limited benefit. While the CTC is a generous benefit for many middle-income families, it phases in with parents' earnings, such that low-earning families and families without earnings receive either a partial credit or no credit at all. And the CTC's refundable component, through which lower-income families receive the credit, tops out at $1,400 per child, substantially less than the $2,000 per child that can be realized by higher-income families. Those who do not receive a full credit include families in which parents are working full-time, full-year at the federal minimum wage, military families, families with younger children, and those without access to steady work – that is, families in vulnerable and precarious positions. In fact, one-third of the families with children in the United States earn too little to get the full $2,000 per child tax credit, including low- and no-income as well as many middle-income families.

For this reason, there are many proposals to reform the CTC, some of which decouple the credit from earnings, while others continue to tie it to earnings. One example of the former is the American Family Act (AFA), to be introduced in this congress by Senators Michael Bennet and Sherrod Brown and Representatives Rosa DeLauro and Suzan DelBene. The AFA is similar in structure to a proposal in the last congress put forward by Senators Bennet and Brown, which we have examined in a previous research brief. The AFA increases the maximum CTC to $3,000 per child aged six to 16[1] and $3,600 per child under six. Critically, it also eliminates the CTC's earnings requirement – guaranteeing children and families with the fewest resources the same credit received by most higher income families.[2] In this brief, we examine how decoupling the CTC from earnings expands its antipoverty impacts by comparing the poverty effects of the CTC expansion proposed in the AFA - when the earnings requirement is eliminated - to its impacts when a form of

1. The House version of the AFA would also make older children eligible. For the purpose of this analysis, we use the Senate version as it conforms to the age parameters of the current Child Tax Credit.
2. The credit we model begins to phase out for single filers with more than $130 thousand in adjusted gross income and joint filers with more than $180 in AGI.

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the earnings requirement is maintained.[3] This brief thus provides evidence for those who seek to understand how an earnings requirement affects the potential antipoverty impacts of expansions to the CTC; the authors of the AFA have specified that the earnings requirement should be eliminated. In order to further examine the effects of benefit levels, the brief also presents results from a model of a less generous version of the credit – $2,000 per child age six to 16 and $3,000 per child under six – with and without an earnings requirement. Our results show that:

- Increasing the credit amounts to those proposed by the AFA and decoupling it from earnings moves approximately **4 million** children out of poverty and **1.6 million** children out of deep poverty, cutting deep poverty among children in half.
- Continuing to tie eligibility to earnings, even with higher benefit levels, meaningfully diminishes the credit's potential effects on both poverty and deep poverty among children.
- The less generous credit that we model that is not tied to earnings has a greater antipoverty impact than the larger credit increase when it is tied to earnings. Put simply, increasing eligibility for the CTC by eliminating the earnings requirement does more to impact the child poverty rate than just increasing CTC credit amounts. But, of course, the combination of higher benefit levels and no earnings requirement does even better.
- **$2 a day poverty among children and families would nearly disappear with a CTC decoupled from earnings, whereas it barely budges with a policy that is predicated on earnings. Deep poverty also barely budges when the credit is still tied to earnings.**

To analyze the effects of various CTC proposals, we use the Annual Social and Economic Supplement to the Current Population Survey, the national household dataset used to calculate annual poverty statistics. We use the Supplemental Poverty Measure (SPM), as this measure counts benefits from the tax system and other non-cash sources, making it a more comprehensive measure of income poverty. We use data from 2018, which calculates poverty for calendar year 2017. Importantly, 2018 tax filers were subject to the tax law before the recent Tax Cuts and Jobs Act, so we begin by simulating the poverty rate supposing that TCJA had been in effect for 2018 filers filing taxes on the basis of their 2017 income. For this reason, our baseline poverty estimates differ from published sources somewhat. Additionally, our baseline estimates of the CTC come from this simulation.

Results

With the Child Tax Credit,[4] 14.9 percent of children (or roughly 10.3 million children) in the United States under age 17 live below the poverty line (see Table 1). As it stands, the CTC brings the national child poverty rate down from 18.1 percent to 14.9 percent and moves roughly 2.2 million children out of poverty. That is, the CTC lifts 1 in 6 previously poor children and their families out of poverty. **If the value of the CTC were to increase to the values proposed in the AFA,[5] and the credit were decoupled from earnings, the poverty rate for children under 17 would fall to 9.3 percent and nearly 4 million additional children[6] would move out of poverty (see Table 1)**. Such a reform would almost triple the number of children that the CTC moves out of poverty, from 2.2 to 6.1 million, meaning that the CTC would cut child poverty nearly in half (see Figure 1).

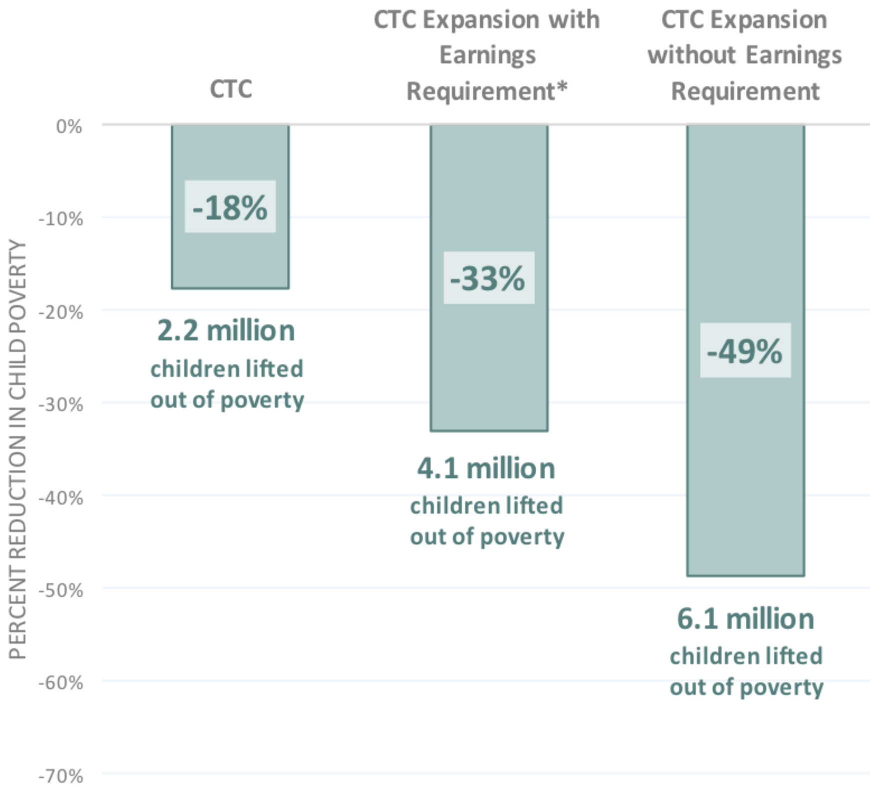
3. The earnings requirement we model is more generous than the one established in the TCJA, as we discuss in the results section.
4. Here, we are referring to the CTC under TCJA tax law. In the TCJA, the maximum credit a family can receive is $2,000 per child. This credit phases in for low-income workers and begins to phase out at $200,000 and $400,000 in earnings for single and joint filers, respectively. The credit is also not fully refundable, so those families whose tax liability is less than their credit value can only receive $1,400 per child in the form a tax refund.
5. $3,000 for older children and $3,600 for younger children.
6. We find that the CTC expansion without the earnings requirement moves 3.9 million children under 17 out of poverty and 4.0 million children under 18 out of poverty (as reported in our research brief on 2020 tax credit proposals).

Table 1: Poverty Impacts of the CTC and CTC Expansions

	Without CTC	*With CTC*	*CTC Expansion with Earnings Requirement**	*CTC Expansion without Earnings Requirement*
Child Poverty Rate (<17) *Number of Children in Poverty (Millions)*	18.1% 12.5	14.9% 10.3	12.1% 8.4	9.3% 6.4
Child Deep Poverty Rate *Number of Children in Deep Poverty (Millions)*	5.0% 3.5	4.6% 3.2	4.1% 2.8	2.3% 1.6
Child Extreme Poverty Rate *Number of Children in Extreme Poverty (Millions)*	1.6% 1.1	1.6% 1.1	1.5% 1.0	0.4% 0.2
Net Costs (with savings from existing Child Tax Credit)	*-$107*	*$107*	*$61*	*$91*

*Under this scenario, we phase in the credit at a rate of 45 percent for each dollar of earnings beginning at the first dollar of earnings.

Figure 1: Poverty Impacts of the CTC and CTC Expansions

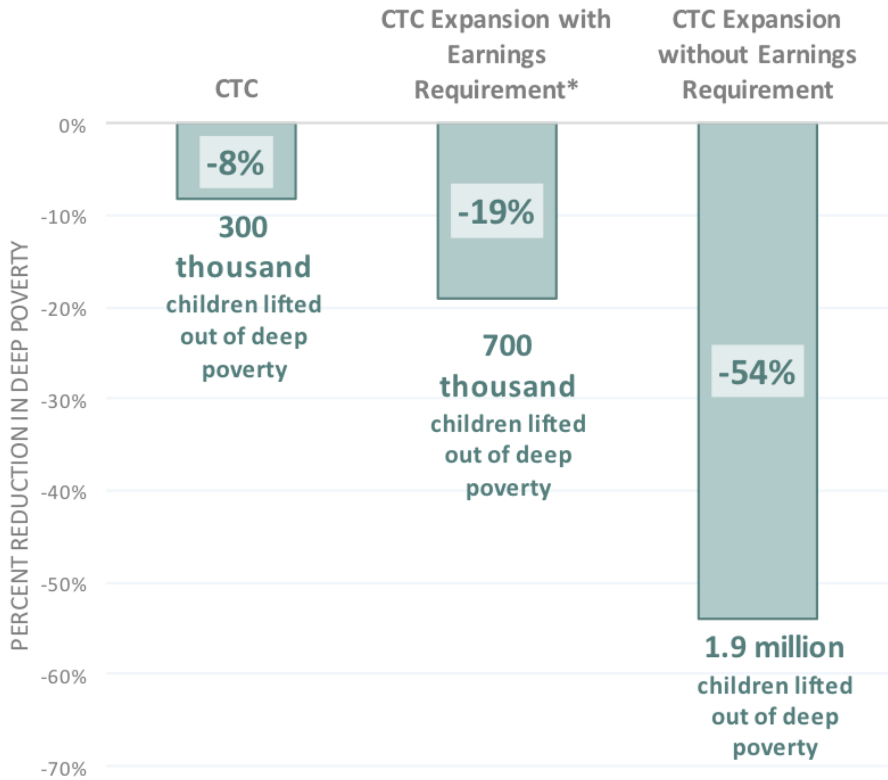


**Under this scenario, we phase in the credit at a rate of 45 percent for each dollar of earnings beginning at the first dollar of earnings.*

If the earnings requirement were maintained, however, the CTC expansion would have a much smaller impact on the child poverty rate: the poverty rate would then fall to only 12.1 percent and only 1.9 million additional children would move out of poverty (see Figure 1). In our model of the CTC expansion with the earnings requirement, we phase the credit in for low-income workers with children at a generous phase-in rate of 45% for each dollar earned - as opposed to current law's 15%. But even with this more generous phase in, a CTC expansion that is still coupled with an earnings requirement would fail to benefit many children in poverty. We acknowledge that reducing child poverty by nearly 3 percentage points, as would happen were the CTC expanded while maintaining its tie to earnings, is no small feat. We also acknowledge that many middle- and upper-middle-income families would also realize some benefit from expanded credit amounts that remain tied to work. Nevertheless, continuing to tie even an expanded credit to earnings would leave many poor, disconnected, and economically precarious families and their children behind.

The consequences of the earnings requirement are even more evident when looking at the impact of the CTC on deep poverty under our two scenarios. A family in deep poverty lives below half of the poverty threshold for their household size. For example, the average poverty threshold for a one-adult, two-child family in the Chicago metro area is $23,494, and the deep poverty threshold is $11,747. As it stands, the CTC does not reach many children in deep poverty; the CTC reduces deep poverty among children from 5.0 percent to 4.6 percent and moves approximately 300,000 children out of deep poverty (see Figure 1). **When the CTC expansion we model is decoupled from earnings, the deep child poverty rate is cut in half—falling from 4.6 percent to 2.3 percent—and an additional 1.6 million children move out of deep poverty (see Table 1). When the earnings requirement is maintained, the CTC expansion's impact on the deep poverty rate is greatly reduced – the poverty rate falls by just 0.6 percentage points, moving only 380,000 more children out of deep poverty (see Figure 2).** Again, while this effect would not be trivial, making the credit available to financially worse-off families and children by decoupling it from earnings would make for much steeper reductions in deep poverty among children.

Figure 2: Impacts of the CTC and CTC Expansions on Deep Poverty



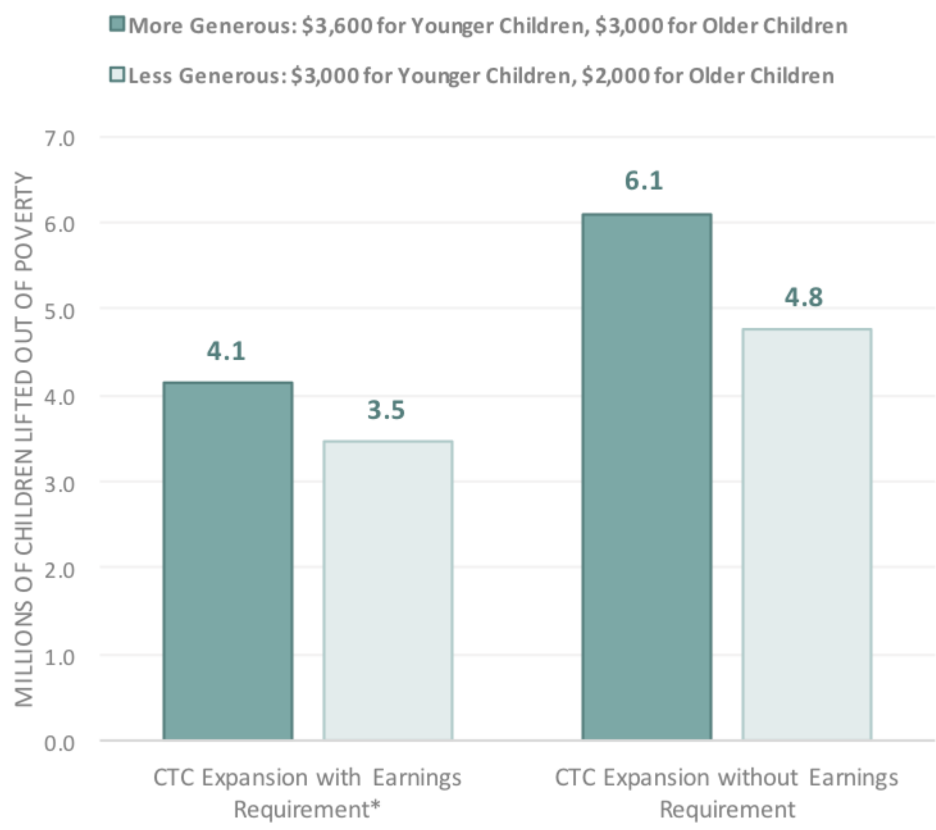
**Under this scenario, we phase in the credit at a rate of 45 percent for each dollar of earnings beginning at the first dollar of earnings.*

Lastly, we look at the predicted impact of the two forms of the credit on extreme poverty (defined as $2 per day, per family member). As is stands, approximately 1 million children in the United States live in extreme poverty, and the CTC does not change the extreme child poverty rate. The CTC expansion modeled here is with a credit that is decoupled from earnings moves 4 out of 5 children (or 900,000 children) out of extreme poverty. That is, **$2 a day poverty among children and families would nearly disappear with a CTC decoupled from earnings, whereas it barely budges with a policy that is predicated on earnings**.[7]

7. One might wonder why any children would remain in extreme poverty if the CTC were decoupled from earnings; the reason has to do with medical-out-of-pocket spending. We determine the predicted impact of the American Family Act CTC expansion on the poverty rate using the Supplemental Poverty Measure (SPM). The SPM improves upon the official measure in a number of ways: (1) it uses post-tax and post-transfer income in its accounting of family resources, (2) it uses a geographically adjusted poverty threshold that varies across the United States according to regional housing costs, and (3) it accounts for household spending on work-out-of-pocket expenses and medical-out-of-pocket expenses. Under the SPM, families with medical-out-of-pocket spending that exceeds their post-tax, post-transfer income will have $0 in family resources, and it is assumed at any additional income they receive will go towards this medical spending until it is paid down. Thus, for some families with high medical-out-of-pocket expenses who are in extreme poverty, the additional income that they receive from the CTC expansion is allocated towards their medical-out-of-pocket expenses, and they and their children therefore remain in extreme poverty.

What matters more for reducing child poverty, the credit amount or eliminating the earnings requirement? The attentive reader will not be surprised by the answer. In Figure 3, we compare estimates of the number of children lifted out of poverty by a CTC expansion to $3,600 per young child and $3,000 per older child **with** the earnings requirement to a less generous credit **without** the earnings requirement. The less generous credit we model has a value of $3,000 per young child and $2,000 per older child (a full set of results from these simulations are presented in the Appendix).[8] When examining these results, we see that the more generous credit, when tied to earnings, moves fewer children out of poverty (4.1 million) than the **less generous credit when it is not tied to earnings** (4.8 million; see Figure 3). This difference is even more pronounced when looking at deep poverty (700 thousand vs. 1.6 million; see Figure 4). Note that the more generous credit modeled with the earnings requirement has a net cost of roughly $61 billion while the less generous credit without the earnings requirement carries a net cost of $37 billion. Nevertheless, the latter does more to curb child poverty while costing less because it expands eligibility to all families and children living below the poverty line. Overall, eliminating the earnings requirement is key to increasing the CTC's antipoverty impacts.

Figure 3: Millions of Children Lifted Out of Poverty by More Generous and Less Generous Credits



*Under this scenario, we phase in the credit at a rate of 45 percent for each dollar of earnings beginning at the first dollar of earnings.

8. See Table A1 for the impacts of the least generous credit that we modeled and Table A3 for impacts of the most generous credit.

Figure 4: Millions of Children Lifted Out of Poverty by More Generous and Less Generous Credits

**Under this scenario, we phase in the credit at a rate of 45 percent for each dollar of earnings beginning at the first dollar of earnings.*

Conclusion

The CTC benefits many families in the United States, but it has consistently left out the children and families who would likely benefit from it the most. Proposals that decouple the CTC from earnings present an opportunity to change that. Of the roughly 12.5 million children who would be in poverty absent the CTC, the current CTC moves 1 of 6 out of poverty. Increasing credit amounts to those proposed in the American Family Act without decoupling the credit from earnings would move 1 in 3 out of poverty, while increasing the credit *and* decoupling it from earnings moves 1 in 2 children who would otherwise be in poverty above the poverty line. Increasing the maximum credit value and decoupling the credit from earnings would transform the CTC into a credit that works for both middle- and low-income families, and in doing so would bring 4 million children out of poverty. Decoupling from earnings would do even more in reducing both deep and extreme child poverty. Even a less generous hike in the credit value alongside the elimination of the earnings requirement would do more to reduce child poverty than a more generous credit tied to earnings. If the earnings requirement is maintained and the credit value increases, then the gains will largely continue to go to middle-income families, and those with the fewest resources will again be left out.

Appendix A

Table A1: Poverty Impacts of the CTC and a CTC Expansion to $3,000 for Young Children and $2,000 for Older Children

	Without CTC	With CTC	CTC Expansion with Earnings Requirement*	CTC Expansion without Earnings Requirement
Child Poverty Rate (<17)	18.1%	14.9%	13.1%	11.2%
Number of Children in Poverty (Millions)	12.5	10.3	9.1	7.8
Child Deep Poverty Rate	5.0%	4.6%	4.1%	2.8%
Number of Children in Deep Poverty (Millions)	3.5	3.2	2.9	1.9
Child Extreme Poverty Rate	1.6%	1.6%	1.5%	0.5%
Number of Children in Extreme Poverty (Millions)	1.1	1.1	1.0	0.4
Cost (Billions)	-$107	$107	$18	$37

*Under this scenario, we phase in the credit at a rate of 45 percent for each dollar of earnings beginning at the first dollar of earnings.

Acknowledgements

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