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The Earned Income Tax Credit Conundrum: The Unintended Exclusion of Latina/o Children

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Introduction

Latina/os constitute the biggest minority-majority in the United States, and a powerful, growing voting force. According to the U.S. Census Bureau, as of 2013, Hispanics made up 54 million of the population.[1] By 2060, the U.S. Census Bureau estimates the population will reach 128.8 million, constituting 31 percent of the U.S. population by then.[2] In 2012, 23.3 percent of elementary and high school students were Hispanic.[3] With exponential growth in population, voting power has also increased for the Latina/o population. In 2006 Hispanics made up 8.6 percent of eligible voters, while by 2010, the percentage had risen to 10.1 percent.[4] A record 25.2 million Latinos were eligible to vote in the 2014 mid-term elections, which made up 11 percent of all eligible votes nationwide.[5] Three-quarters (74 percent) of Latina/o eligible voters are U.S. born[6], and 26 percent are immigrants who hold U.S. citizenship.[7] With the percentage of Latina/o voters dramatically increasing and with continued growth expected, issues pertinent to Latinos must be addressed, otherwise elected officials may not be supported in future elections. Social issues such as immigration are prominent headlines nowadays.[8] Economic issues in the Latina/o community are often overlooked. One such issue with tremendous political and economic impact is the Earned Income Tax Credit (EITC) and its effects on Latina/o children, and their parents/guardians. In particular, the issue that is often overlooked is the current exclusion of children of undocumented parents, a majority of whom are Latina/o children, from the benefits of the EITC through their parents. This paper is aimed at presenting the historical background of the EITC, identifying the current issue as it relates to the Latina/o community, examining how this exclusionary effect exists, proposing changes to eligibility requirements that should be considered to remedy this exclusion, and help break the cycle of poverty for thousands of children.

Federal EITC

EITC History

The idea of the EITC first emerged in the 1960s during debates regarding the issue of poverty. On August 1969, President Richard Nixon proposed the Family Assistance Plan (FAP), which was designed to guarantee cash income to all families as an alternative to public assistance (e.g., welfare). The objective behind this proposal was to "ensure an income foundation throughout every section of America for all parents who cannot adequately support themselves and their children."[9] Despite initial support, FAP failed. In 1974, Senator Russell Long developed an alternative proposal from FAP—a tax credit for employed, low-income taxpayers.[10] In essence, this was considered a government sponsored "work bonus."[11] Initially this proposal was rejected by the House of Representatives, but as a result of President Ford's call for stimulative tax cuts, Congress eventually enacted Senator Long's proposal as part of the Tax Reduction Act of 1975.[12] This "work bonus" became known as the Earned Income Tax Credit (EITC). The EITC was described by the Senate committee report in the following manner:

> This new refundable credit will provide relief to families who currently pay little or no income tax. These people have been hurt the most by rising food and energy costs. Also, in almost all cases, they are subject to the social security payroll tax on their earnings. Because it will increase their after-tax earnings, the new credit, in effect, provides an added bonus or incentive for low-income people to work, and therefore, should be of importance in inducing individuals with families receiving Federal assistance to support themselves. Moreover, the refundable credit is expected to be effective in stimulating the economy because the low-income people are expected to spend a large fraction of their increased disposable incomes.[13]

Undocumented immigrants constitute 11.9 million individuals in the United States, which remains an ongoing political and policy issue. About three-quarters of the undocumented population are Latina/os.[29] Many of these undocumented individuals are also married to U.S. citizens or residents aliens, creating a "mixed-status" family.[30]

In 1986, EITC was made permanent through the Tax Reform Act of 1986 thus demonstrating President Reagan's emphasis on EITC's importance. Although the credit helped families prior to Tax Reform Act of 1986, there were concerns that inflation reduced the value of the credit.[14] Moreover, given the increase of income due to inflation, many families that needed the credit were no longer eligible for it.[15] Through the Tax Reform of 1986, President Reagan proposed to increase the EITC, and index it for inflation in future years.[16]

EITC expansion between 1984 and 1996 boosted the work effort of parents, particularly single mothers. Single mothers accounted for more than half of the large increase in employment among Americans during that period.[17] The most significant gain in employment attributable to EITC occurred among mothers with young children and mothers with low education. [18] According to University of Chicago economist Jeffrey Grogger, EITC expansions in the 1990s "appear to be the most important single factor in explaining why female family heads increased their employment over 1993–1999."[19]

EITC Today & the Issue

EITC today is often referred to by policy makers as the "nation's largest federal anti-poverty program."[20] In 2010, the EITC lifted roughly 5.4 million people out of poverty, including 3 million children.[21] The EITC has been credited for improving the lives of poor children and promoting work. Today, in order to qualify for the EITC, individuals must care for a qualifying child, along with personally meeting statutory criteria. A qualifying child must meet all of the following tests: 1) age, 2) relationship, 3) residency, and 4) joint tax return.[22] The age criterion states that, by the end of the tax year, the qualifying child must either be under the age of 19 or be a full-time student under the age of 24. The relationship criterion is defined as the child being the son, daughter, stepchild, eligible foster child, or a descendant of the taxpayer. To satisfy the residency requirement, the child must have lived with the taxpayer in the United States for more than half the year. Finally, for the joint tax return test, the child must have not filed his/her own tax return.

After determining if the taxpayer parent has a qualifying child, he/she must then meet statutory criteria required to be able to claim this credit. To claim EITC on a personal tax return, a parent must have a Social Security Number that is valid for employment, must have earned income by working for someone else or running a business, and must be a full-time U.S. citizen or resident alien.

The criterion about the parents' full-time U.S. citizenship or resident alien status is what presents the issue that affects Latina/o children. Section 7701(b)(1)(A) of the Internal Revenue Code (IRC) presents three tests to determine if an individual qualifies as a resident alien: i) a green card test, ii) election test, and iii) a substantial presence test.[23] Under the green card test, an individual is considered a resident alien from the day that he or she is admitted to the United States as a lawful permanent resident (that is, given a "green card") until the day that this status is officially revoked or judicially found to be abandoned.[24] While the alien officially has lawful permanent resident status, he or she is considered a US tax resident even while living outside the United States.[25] Under the substantial presence test, an individual must meet the following conditions to be considered a resident alien: i) he or she must be physically present in the United States for thirty-one days in the current year; ii) He or she must be physically present in the United States for a weighted average of 183 days over a three-year testing period that comprises the current and the two preceding years.[26] Days of US presence are computed under a weighting formula that counts the following non-exempt days of presence: i) all days in the current year, plus ii) one-third of the days in the preceding year, plus iii) one-sixth of the days in the second preceding year.[27] If the alien has been lawfully admitted in the U.S. for permanent residence, he or she is a resident alien.[28] Therefore for the purposes of the EITC credit, undocumented individuals are not considered resident aliens.

Undocumented immigrants constitute 11.9 million individuals in the United States, which remains an ongoing political and policy issue. About three-quarters of the undocumented population are Latina/os.[29] Many of these undocumented individuals are also married to U.S. citizens or residents aliens, creating a "mixed-status" family.[30] The undocumented status of one spouse bars the married couple from receiving the benefits of the EITC.[31] Seventy-three percent of undocumented immigrants, or mixed-status families' children are born in the U.S., making them citizens of this country.[32]

The number of U.S. born children in mixed-status family has expanded from 2.7 million in 2003, to 4 million in 2008. Given the requirements to receive EITC, these 4 million, which 3 million are Latina/o children, are not receiving the benefit that they are meant to receive, due to their parents' legal status as undocumented immigrants. The EITC is

Studies also show that children of families with more income from refundable credits will do better in school, and are more likely to attend college, and earn more as adults — likely breaking the cycle of poverty.[38] Furthermore, those same children are more likely to avoid the earliest onset of disabilities, and other illnesses associated with child poverty.[39]

intended to have salutary effects of lifting families out of poverty, yet millions of children who are supposed to benefit from this credit are remaining below the poverty level.

The only alternative is an illegal one, to file as head of household. Having to choose between filing fraudulently in their tax return, or give up thousands of dollars that they should be receiving for their children is a difficult decision for parents, and one that arguably, they shouldn't have to make.

EITC Recommendations

Increase the Eligibility of EITC
Given this incidental, yet critical exclusion of benefits to millions of Latina/o children, it is imperative that changes in the EITC eligibility be implemented. President Obama has discussed policy changes on the EITC, but none addressing this exclusion of U.S. children whose parents are undocumented. In March 2014, President Obama made an announcement about his intention of expanding the EITC.[33] His proposal called to address the problems with the current childless worker EITC, recommended the maximum credit to about $1,000, and suggested increasing the income level at which the credit is fully phased out at $18,000.[34] Although this will help lift many children out of poverty, Latina/o children with undocumented parents will still be deprived of this benefit.[35] This deprivation affects more than just household income, there are implications for education and public health. According to the Center on Budget and Policy Priorities, the EITC's income-boosting measures improve education outcomes for young children in low-income households.[36] For every $1,000 increase in annual income for children ages two to five years, school performance on variety of measures, including standardized test scores, improves.[37] Studies also show that children of families with more income from refundable credits will do better in school, and are more likely to attend college, and earn more as adults — likely breaking the cycle of poverty.[38] Furthermore, those same children are more likely to avoid the earliest onset of disabilities, and other illnesses associated with child poverty.[39]

With millions of Latina/o children missing out on this critical economic education and health resource, it is time to change the criteria needed to receive this credit. The burden shouldn't be on the parent per se, it should also be on the status of the child. If the child is a qualifying child, then the parent, regardless of his/her legal status, should be able to receive that tax credit for the sake of the child. By making the criterion rest on the child alone, and not the parent, it would be harmonious with the legislative intent of the bill, lifting children out of poverty. To receive the EITC, the child must be a U.S. citizen, national, or resident alien (which includes those with temporary status such as beneficiaries of the Deferred Action for Childhood Arrivals program).

Rebutting Misconceptions
The proposed expansion of the EITC wouldn't be without opposition. Giving money to undocumented parents of children with lawful status in this country is often seen as giving money to those who do not contribute to the U.S. economic system.[40] Although this misconception is mainstream, it is without merit. Undocumented parents are subject to paying federal, state, and local consumption taxes, along with any applicable federal, state, local income taxes.[41] Undocumented parents also pay a higher effective income tax rate when compared to the average American taxpayer, due to the not being eligible for credits that a regular taxpayer is entitled to. [42] Many undocumented parents, like many U.S. citizens, pay their federal and state income taxes through wage withholding.[43] To receive a refund of any overpayment of their federal and state income taxes, they are required to file tax returns requesting refunds. However, undocumented immigrants must file their tax returns with an ITIN because they do not qualify for a SSN.[44] Because of the misperception of abuse of this number, obtaining an ITIN is not a simple task. Whereas a SSN is issued to all U.S. citizens immediately at birth, an ITIN must be obtained through an onerous application process requiring original identification documents, which might not be readily accessible.[45] The difficulty in obtaining an ITIN, combined with the lack of access to and intimidation by federal state and local income tax systems and government officials, results in millions of undocumented immigrants simply not filing tax returns.[46] Therefore, these taxpayers have very likely overpaid their federal and state tax liabilities.[47]

Another consideration should be on the long-term consequences by not imposing this change. As alluded to earlier, poverty stricken children benefit from their parents receiving the EITC. Depriving this group of children access to the EITC, ensures they are deprived of the health and educational benefits derived by this credit. For children in low-income families, a $3,000 increase in family income between a child's prenatal year and his/her fifth birthday results in an average of 17 per-

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cent increase in annual earnings and an additional 135 hours of work when they become adults.[48] By not investing in this group of children that are deprived of the EITC, we are not giving them a chance to succeed. They may end up becoming another statistic, dependent on government programs in their adulthood. Wouldn't we rather invest as them as kids, and have them pay back into the system once they are adults?

Conclusion/Policy Benefits of Expanding EITC

The EITC has long provided supplemental income for low-income taxpayers. This credit is not a merely a giveaway, it requires that taxpayers enter the workforce. The EITC has arguably been a successful program in lifting many families out of poverty. However, the EITC is not without its flaws. Millions of children that should be benefitting from this credit are excluded because of their parents legal status (or lack thereof) in this country. Although the recent Deferred Action for Parents of Americans and Lawful Permanent Residents (DAPA) executive order will provide undocumented parents with valid SSNs, and enable them to claim the EITC to help their children, many other children whose parents do not qualify to receive a SSN under the new immigration executive order, will be deprived of this benefit. The EITC is meant to help lift children out of poverty, and put them on equal footing with their counterparts. With the current statutory criteria of the EITC, this is not possible, and expansion for the requirements to be eligible for the EITC should be implemented. Without it, millions of American children, in particular those of Latina/o decent, will be deprived of this crucial benefit.

Endnotes

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