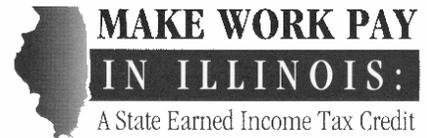


The Illinois Earned Income Tax Credit: Preserved and Improved in 2003



State policymakers expanded a critical support for working families

The state Earned Income Tax Credit (EITC), established in 2000, was renewed and improved during the 2003 legislative session. Last year, the state EITC provided a \$44 million benefit to 584,000 low-income, working families. Beginning in tax year 2003, the state EITC will help 150,000-200,000 more working families with about \$23 million in additional benefits by drawing upon federal funding, reflecting policymakers' choice to make the state EITC "refundable" as well as permanent.

A permanent EITC helps provide income stability.

A permanent credit provides families who are working towards self-sufficiency with increased income stability. It shows Illinois' commitment to supporting families who, despite the fact that they work, still struggle to make ends meet.

A refundable EITC supports an additional 150,000-200,000 families.

The state EITC established in May 2000 did not reach the lowest-income workers – approximately 25 percent of Illinois working families who receive the federal EITC – because it was non-refundable.

The refundable credit approved by legislators in 2003 will reach the 150,000-200,000 working families who, in the example of a four-person household, have incomes below \$8,000 (Illinois' income tax threshold for a family of that size). Refundability simply means a taxpayer gets the full value of the credit, even if the credit exceeds his or her income tax liability. Making the credit refundable recognizes the real tax burden for low-income workers comes from sales, property, excise and payroll taxes, not income taxes.

Example 1: A minimum-wage family of four – earning \$10,700 yearly – qualifies for a \$204 Illinois EITC. Under the original state EITC policy, that family only realized an \$81 benefit, covering their state income tax liability. They lost the remaining \$123. By making the credit refundable, this same family will receive a refund check for the remaining \$123 to reimburse them, at least partially, for the other taxes they pay.

Example 2: A family of four that earns \$8,000 annually pays no state income taxes. Under the original policy, they received no benefit from the non-refundable EITC. With refundability, that family will now receive a \$160 refund check, mirroring the approach of the larger, federal EITC.



An improved EITC benefits local economies.

The additional purchasing power that results from the EITC brings income into the community and helps families in the process of asset-building. Families in every Illinois county receive the EITC.

Our work is not yet done.

By increasing the state credit to 20% of the federal credit in the years ahead, Illinois would be able to join 22 other states that do not tax families and individuals with incomes below the poverty level. Currently, Illinois has the smallest state credit available, set at 5% of the federal credit.

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Frequently Asked Questions

What do *refundable* and *non-refundable* mean?

- Refundable: If the credit is larger than a family's income tax bill (tax liability), the family receives a refund check equal to the difference between the calculated credit and the taxes owed. This is how the federal credit and most other state credits work.
- Non-refundable: The credit can only offset the family's income tax bill. Even if the amount of the calculated credit exceeds the tax liability, the family does NOT receive a refund.

How do the state and federal EITC relate?

- The Illinois EITC piggybacks on the federal credit in that Illinois uses federal eligibility rules to determine whether a family is eligible for the state EITC.
- Illinois sets its credit as a percentage of the federal credit (currently 5%).

How does Illinois' tax threshold (income level at which taxes are owed) compare with other states?

Even with the help of the state EITC, Illinois has the 11th lowest tax threshold in the nation.

	<u>Illinois</u>	<u>States' Average</u>
Tax Threshold (including EITC)	\$14,300	\$23,187
% of Poverty	79%	128%

- Without the state EITC, a two-parent/two-child family would begin paying income taxes at \$8,000 of earned income (assuming no property tax or other credits).
- With a 5% Illinois EITC, the four-person family begins paying income taxes to the state at \$14,300 of earned income. In other words, the 5% state EITC offsets the family's entire tax liability up \$14,300 of earned income.

How does the Illinois tax threshold compare with the federal tax threshold?

Without the EITC, the tax threshold for a four-person family (two parents, two children) is \$23,850 lower in Illinois than at the federal level.

	<u>Illinois</u>	<u>Federal</u>
Tax Threshold* (NOT including EITC)	\$8,000	\$31,850
% of Poverty	44%	176%

*Tax thresholds reflect standard deductions, exemptions and general tax credits except the Earned Income Tax Credit.

How does the EITC fare outside of Illinois?

- The number and value of refundable state EITCs have increased in the last three years.
- On the national and state levels, the EITC has strong bipartisan support and the endorsement of business as well as social service advocates.
- Eleven of the 17 states (or localities) with an EITC – Colorado, the District of Columbia, Indiana, Kansas, Maryland, Massachusetts, Minnesota, New Jersey, New York, Vermont and Wisconsin – offer refundable credits.

How can the state EITC be further improved?

- A state EITC set at 20% of the federal credit would increase Illinois' income tax threshold to the poverty level.
- An increase in the state EITC can be accomplished in one year or be phased in over a three-year period, with a 5% increase each year.