

Expanding the Earned Income Tax Credit For Youth Formerly in Foster Care¹

THE PROBLEM

Across the United States, approximately 20,000 to 25,000 youth between ages 18 and 21 age out of foster care each year.² Young people exiting the foster care system often endured instability, neglect or abuse, making the path to successful, independent adulthood more challenging than the path for their non-foster peers. As a result, youth exiting the foster care system experience a range of poor outcomes including higher rates of mental illness, lower educational attainment and lower incomes. By age 24, youth formerly in foster care earn between half and a quarter of the earnings of their non-foster peers.³ These individuals face additional barriers to economic stability and other challenges such as a lack of stable housing, limited access to necessary documentation and fewer concrete supports as they transition into adulthood.⁴

By age 24, nearly 30% of youth formerly in foster care have experienced at least one night of homelessness.
(Source: Chapin Hall Issue Brief, Partners for Our Children)

The Employment Picture⁵		
Age 23/24	Former Foster Youth	General Population
Currently Employed	48.0%	75.5%
Median Hourly Income	\$10.38	\$13.19
Median Annual Income	\$8,791.00	\$20,110.00
Has a savings or checking account	47.30%	85.10%
Report not enough \$ to pay rent	28.5%	7.4%

The Earned Income Tax Credit (EITC) is a federal tax credit for low- and moderate-income working individuals and families. The credit was first established in the 1970’s as an alternative to a negative income tax and has grown to become one of the most important federal anti-poverty programs. Research has consistently shown the EITC brings recipients into the labor market and reduces poverty.⁶ The credit is both variable, meaning the amount

¹ For the purposes of this policy proposal, we will define “youth formerly in foster care” as individuals formerly in care or individuals in extended care.

² The AFCARS Report, Department of Health and Human Services, Administration of Children and Families, July 2014. <<http://www.acf.hhs.gov/sites/default/files/cb/afcarsreport21.pdf>>

³ Chapin Hall Issue Brief, Partners for Our Children, University of Chicago, 2012. <http://www.chapinhall.org/sites/default/files/publications/Midwest_IB3_Employment.pdf>

⁴ Center for the Study of Social Policy (2014). Support Youth Transitioning from Foster Care. Policy for Results.

⁵ Midwest Evaluation of the Adult Functioning of Former Foster Youth: Outcomes at Ages 23 and 24; Chapin Hall, 2010.

⁶ Center for Budget and Policy Priorities, 2004. Earned Income Tax Credit Promotes Work, Encourages Children’s Success at School, Research Finds For Children, Research Indicates That Work, Income, and Health Benefits Extend Into Adulthood, Center for Budget and Policy Priorities, April 15, 2014.

of the credit changes, and refundable, meaning that an individual can receive more federal support than he/she pays in taxes. The variability component is designed to incentivize work and raise living standards. In order to claim the credit a taxpayer must have earned income. The credit rises with earned income until it reaches a maximum and then begins to phase out.⁷ The credit provides significant support to low-income parents, but the maximum credit that can be claimed by a childless worker over 25 years of age is approximately \$500.⁸

“I’ve been financially independent for several years now and it’s stressful...knowing you can’t splurge every now and then because you have no financial support.” (Source: Guardian Scholars, UCLA)

The EITC is not currently offered to adults under age 25 unless they are parenting. The current policy assumes that many adults ages 18 to 24 earn little income but continue to rely on their parents for financial support. While this may be true for some young adults, this is almost never true for youth formerly in foster care. At 21, only 13.2 percent of youth formerly in foster care report living with a biological or foster parent.⁹ Expanding the EITC would provide a benefit to this population that

could help reduce poverty and increase labor market participation with very little additional cost to the taxpayer. Youth formerly in foster care are particularly vulnerable and deserve the benefits associated with poverty programs for adults.

THE OPPORTUNITY

The U.S. government has a bipartisan legacy of leadership on child welfare reform. In recent years Congress has made substantial progress toward improving the lives of vulnerable young people, building momentum for continued reforms. In 2005, Congress passed the Deficit Reduction Act, which included investing \$100 million over five years for courts to track cases, provide training and increase collaboration with child welfare agencies. In October 2008, the Fostering Connections to Success and Increasing Adoptions Act was unanimously passed in Congress and signed into law by President Bush.¹⁰ This was the most significant child welfare legislation in ten years.

Recently, President Obama and Members of Congress on both sides of the aisle have expressed an interest in reforming the tax code and expanding the EITC. More specifically, President Obama and Congressman Ryan have both proposed doubling the maximum credit, phase-in and phase-out rates for childless workers and lowering the eligibility age for workers from 25 to 21 years of age. The 114th Congress presents a moment of opportunity to expand the EITC for youth formerly in foster care ages 18 to 25 and an expansion of the

⁷ Earned Income Tax Credit Promotes Work, Encourages Children’s Success at School, Research Finds For Children, Research Indicates That Work, Income, and Health Benefits Extend Into Adulthood, Center for Budget and Policy Priorities, April 15, 2014.

⁸ The term “childless worker” includes non-custodial parents, meaning a parent who does not have physical or legal custody of his/or her child.

⁹ Midwest Evaluation of the Adult Functioning of Former Foster Youth: Outcomes at Ages 21; Chapin Hall, 2007.

¹⁰ The Commission on Children in Foster Care, Pew Charitable Trust.

<<http://www.pewtrusts.org/en/archived-projects/commission-on-children-in-foster-care>>

credit to other young adults ages 21 to 25. This policy should be incorporated into the overall tax reform efforts. It not only will provide much needed financial support to those in need, but it will also incentivize work and equip youth formerly in foster care to become successful adults and productive members of society.

THE POLICY SOLUTION

According to the Center on Budget and Policy Priorities, “because childless workers face tax burdens that exceed their small credits, they are the lone group that the federal tax system taxes into, or deeper into, poverty. In 2012, federal income and payroll taxes pushed 1.2 million childless workers into poverty and another 5.8 million *deeper* into poverty.”¹¹ The EITC is one of the nation’s most effective tools for reducing poverty, and low-income individuals without eligible children need access to benefits like the EITC for support.

In 2013, the EITC lifted 6.5 million people out of poverty by providing an average credit of around \$2,400. (Source: Internal Revenue Service, Statistics for Tax Returns with EITC)

We recommend expanding the EITC to youth ages 18 to 25 formerly in foster care and to other young adults ages 21 to 25; and increasing the size of the credit and phase-out rates for childless workers.

Including these individuals as eligible for this benefit will encourage employment and establish patterns of workforce participation that will continue throughout their lives.¹² This paper outlines the details of the policy initiative including setting eligibility standards, developing a tracking mechanism and implementation plan, increasing the annual credit and estimating costs.

Setting Eligibility: Defining “Youth Formerly in Foster Care”

Foster care is intended as a temporary intervention where children are cared for while the child welfare system can identify a suitable permanent living situation for the child. As children age, their chances of finding a stable, permanent home drop precipitously, and older youth in care are at risk for a range of negative outcomes including low income, homelessness and imprisonment. For example, Chapin Hall’s Midwest Study found nearly 25 percent of foster youth had not obtained a high school diploma or General Educational Development (GED) diploma by age 23 or 24 compared with just seven percent of youth in the general population.¹³

¹¹ CBPP analysis of the Census Bureau’s Current Population Survey using the Supplemental Poverty Measure, which includes the cash value of tax credits and benefit programs such as SNAP. See Marr et al.

¹² The President’s Proposal to Expand the EITC, Executive Office of the President, U.S. Department of Treasury, March 2015.

¹³ Midwest Evaluation, 2010.

We recommend defining “youth formerly in foster care”, for the purposes of this policy proposal, as individuals who were in care on or after their 16th birthday.

Under the proposed policy, working youth ages 18 to 25 could claim the EITC if they were in the child welfare system and under court jurisdiction on or after their 16th birthday.

There are several reasons to set age 16 as the standard for eligibility and age 18 as the age at which an individual could claim the credit. Research and U.S. policy recognize the importance of providing transition services to youth starting before age 18 and continuing past their 18th birthdays. For example, the Jim Casey Youth Opportunities Initiative offers youth between ages 14 and 24 a matched savings account to promote saving and asset building. Likewise, eligibility for the federal Chafee Education Training Voucher is set at age 16 and many states offer Chafee services at age 16 or earlier.¹⁴ Keeping the eligibility age of 16, an age commonly used for Chafee services eligibility among states, reduces the likelihood of confusion that could lead to accidental claims among ineligible youth.

Setting eligibility lower than 18 years of age also removes a perverse incentive. Stacking the eligibility for multiple benefits at age 18 discourages older youth from seeking permanent options such as guardianship, adoption or reunification with biological parents. Finally, this eligibility standard captures a large portion of the most vulnerable youth. According to point-in-time data collected by the Adoption and Foster Care Analysis and Reporting System (AFCARS), approximately 24,600 youth exited care between ages 18 and 20 in 2013. Another 24,200 youth exited care between ages 16 and 17.¹⁵ This standard of eligibility allows for a significant impact while remaining cost effective for the American taxpayer.

Tracking Individuals: IRS Verification

Expanding the EITC to youth formerly in foster care will require a mechanism for the Internal Revenue Service (IRS) to confirm that individuals were in fact eligible for the benefit. This process is complicated by the absence of a federal database that the IRS could use to verify that an individual was in foster care and eligible for the EITC. Therefore, the second-best method involves youth providing verifiable evidence of their experience in foster care that can be audited by the IRS. There is existing precedence for this type of information sharing; providing evidence of eligibility for a benefit is a common approach in applying tax benefits. This strategy goes further, allowing for verification of youth eligibility through the Statewide Automated Child Welfare Information Systems (SACWIS) that monitor youth.

We recommend youth formerly in foster care use their state identification number and/or Social Security Number for IRS verification of eligibility.

Youth may possess a range of documents that can demonstrate child welfare involvement at or after age 16. As part of the EITC application, youth would submit their State ID number

¹⁴ Getting to Good Foster Youth Student Data, California College Pathways.

¹⁵ The AFCARS Report, Department of Health and Human Services, Administration of Children and Families, July 2014. <<http://www.acf.hhs.gov/sites/default/files/cb/afcarsreport21.pdf>>

and/or Social Security number and the state in which they were last in care. If a youth were selected for an audit, the IRS would contact the youth's county or state child welfare agency and confirm eligibility. If the state cannot confirm eligibility, the youth would then have the opportunity to submit documentation demonstrating eligibility directly to the IRS. Relying on the audit system ensures the policy does not create an undue burden on the IRS or create a new level of bureaucracy.

Implementation of the Program

An implementation plan will be required in order to ensure youth formerly in foster care are aware and take advantage of this new benefit.

We recommend a two-year strategic public relations campaign to ensure youth are aware of the benefit and a two-year technical assistance program to ensure case workers are properly equipped to help youth take advantage of the benefit.

The public relations campaign would be conducted during the first two years of the program during tax season. The campaign would take advantage of existing structures and relationships, encouraging organizations with existing programs for foster youth to build awareness and assist with tax filing. Information about EITC eligibility would be included in financial literacy classes. Tax preparers and tax software would mention this potential benefit for youth formerly in foster care, including programs that support low-income individuals filing their taxes, like Volunteer Income Tax Assistance (VITA).

A two-year technical assistance program for case workers would ensure they are fully prepared to properly assist youth in taking advantage of the program. Eligibility for the EITC would be included in the list of benefits to be discussed and documented during transition planning meetings when youth exit care. In addition, state agencies would be required to provide a one-page information sheet on the benefit and how to apply.

Increasing the Credit and Raising the Phase-out Level

The current EITC for childless workers isn't sufficient, with a maximum of about \$500. In addition, the credit phases out at very low rates. This provides little assistance to those in poverty and does not sufficiently incentivize entry into the workforce.

"Increasing the credit for childless workers to an amount closer to that for families with children would augment the direct work incentive and help counter poverty among the working poor." (Source: Glenn Hubbard, former President George W. Bush Economic Advisor)

We recommend doubling the maximum credit to approximately \$1000 and increasing the income level at which the credit is phased out to approximately \$18,000.

These proposed changes have bipartisan support and are consistent with both *The President's Proposal to Expand the EITC*¹⁶ and Congressman Paul Ryan's Plan, *Expanding Opportunity in America*.¹⁷ It is also important to note that taking advantage of this benefit would not disqualify youth formerly in foster care from other benefits available to them in states where care is extended beyond age 18.

Estimated Program Costs

In order to produce a strong cost estimate, we recommend the Government Accountability Office (GAO) conduct a report to determine the overall costs and direct benefits of this policy. That estimate will serve as the primary number as policymakers consider this proposal.

In the interest of comprehensiveness, this paper includes a rough cost estimate. Based on AFCARS data, we estimate that approximately 38,500 young people would become eligible for this expanded credit each year. Because there are seven cohorts that are eligible between 18 and 24, that means around 270,000 young people could claim this credit each year. However, a significant number of youth are custodial parents and can already claim the EITC. Moreover, some youth currently do not work and therefore cannot claim the credit. Discounting those youth, we estimate a likely maximum number of claimants at 135,000 each year. If the EITC is expanded to all youth ages 21 and older and only foster youth receive the benefit from 18 to 21, we estimate a maximum of 98,000 annual claimants under this policy. Again, this is a high estimate as many youth may choose not to file a tax return or may not claim the EITC even if eligible.

In estimating cost we use the credit increases proposed by President Obama and Congressman Ryan. We estimate this would cost a maximum of \$120 million per year. If part of a larger expansion of the EITC proposed by President Obama and Congressman Ryan, this would cost no more than \$57 million per year.

Importantly, both estimates comprise a very small portion of the overall EITC. The U.S. government spent approximately \$66 billion on the EITC in 2013.¹⁸ Even the larger of the two expansions would add less than 0.2 percent to the total cost of the EITC.

In addition to the costs of the program, we also recommend including a small increase in funding for the public relations campaign and technical assistance program as a part of implementation and any bureaucratic work associated with including a new group of individuals eligible for the EITC. We anticipate this to cost approximately \$1 million annually for the first two years of the expansion.

¹⁶ The President's Proposal to Expand the EITC, Executive Office of the President, U.S. Department of Treasury, March 2015.

¹⁷ Expanding Opportunity in America, A Discussion Draft for the House Budget Committee, July 24, 2014.

¹⁸ EITC and Other Refundable Credits, The Internal Revenue Service, Department of Treasury, January 2015. <<http://www.eitc.irs.gov/EITC-Central/abouteitc>>

CONCLUSION

The EITC is among the strongest tools for reducing poverty and encouraging workforce participation. The poverty rate has declined by nearly 40 percent since 1967, in part because of programs like the EITC.¹⁹ President Reagan called it “the best antipoverty, the best pro-family, the best job creation measure to come out of Congress.”²⁰ This is a policy area where Republicans and Democrats have come together to highlight the tremendous benefits of the EITC and to make the case for its expansion.

The Administration, Republican and Democratic leadership in Congress and experts in tax reform and child welfare are in agreement – now is the time to expand the EITC to those who need it most. This is a critical investment in our country’s future and there is no more important goal we can share than ensuring the most vulnerable members of our society have an opportunity to succeed.

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¹⁹ The President’s Proposal to Expand the EITC, Executive Office of the President, U.S, Department of Treasury, March 2015.

²⁰ The Chicago Tribune, October 23, 1986.