



From Refunds to Assets

Leveraging the Benefits of the Earned Income Tax Credit

Trinh Nguyen, a 44-year old single mother who emigrated from Vietnam ten years ago, earns around \$15,000 a year as a seamstress in one of Seattle's garment factories. She lives with her two children in one of Seattle's public housing communities, though she hopes one day to be able to buy a house.

In 2002, she received a flyer—in Vietnamese—from a local nonprofit that explained that she might qualify for the Earned Income Tax Credit (EITC). The flyer directed her to a Volunteer Income Tax Assistance (VITA) site at a nearby community center. Nguyen said she was “amazed” by what the volunteer told her—she would receive more than \$3,500 in the form of a refund check from the federal government. “It was a lot of money,” said Nguyen. “We were able to use it to fix our car and still save some of it for our house.” For Trinh Nguyen, the EITC adds significantly to the \$20-\$30 dollars a month she can normally afford to set aside and

has helped her to build nearly \$7,000 in savings towards the down payment on a small condo in Seattle's International District.

Every year, approximately 20 million lower-income households receive tax refunds through the EITC. The average EITC refund is around \$1,700; some are as high as \$4,000. The EITC is now the largest federal program to help the working poor, and removes more children from poverty than any single federal program.¹ Yet estimates suggest that more than 4 million households that are eligible for the credit fail to claim it.² Data from the 2001 National Survey of America's Families show large disparities in who knows about the EITC, disparities that are magnified when it comes to who files for the credit (Figure 5.1).

Because of the EITC's effectiveness in reducing poverty, a number of efforts have been launched to expand awareness of the credit. The Internal Revenue Service promotes free

Figure 5.1 *Knowledge of the EITC among Low-Income Households (percent)*

	Heard of the EITC	Received the EITC
All	58.1	38.6
Race		
Hispanic	27.1	14.6
Black, Non-Hispanic	68.0	44.3
Other	73.5	51.5
Education Level		
Less than High School	39.8	20.4
High School Graduate	65.0	47.1
Some College	71.4	50.9
College +	64.8	37.3

Source: Maag, Elaine (2005). “Paying the Price? Low-Income Parents and the Use of Paid Tax Preparers,” *New Federalism Working Paper* No. B-64, Washington, D.C.: The Urban Institute.

Low-income households include those earning less than 200% of the federal poverty line.

tax preparation for low-income tax filers through its VITA program. Local community organizations can sponsor VITA sites, and the IRS provides free training for the volunteers, free electronic filing software, and bulk quantities of forms and publications. Financial institutions often partner with VITA sites to offer low-cost bank accounts to EITC eligible families. Foundations and non-profits have also developed

campaigns around the EITC. For example, the Annie E. Casey Foundation launched the National Tax Assistance for Working Families Campaign (NTA) in 2003 to increase EITC filings across the nation. The program doubled the number of families that received free tax preparations at NTA sites, from 97,000 in 2003 to nearly 160,000 in 2004.³ Not only do these programs provide free tax help and information about

San Francisco's Working Families Credit

Box 5.1

In 2003, San Francisco residents failed to claim approximately \$12 million in EITC refunds, money that could have been spent to boost the local economy and to defray the high costs of living in the city. In order to raise the visibility of the EITC in the city and to get more eligible residents to claim their refund, Mayor Gavin Newsom has taken the bold step of offering an added local incentive—the Working Families Credit.

The Working Families Credit works like this: San Francisco residents with dependent children who claim the EITC on their federal income taxes will be eligible to receive an additional payment from the city, probably somewhere between \$200 and \$300.¹ During the 2004 tax season—the first year of the pilot program—over 10,000 San Francisco families claimed the Working Families Credit.

What's unique about the Working Families Credit is that it relies on a public-private partnership to make it work. Taking the city's tight budget into account, Mayor Newsom earmarked \$3 million dollars from the city's general fund for the two-year pilot program, and is turning to the business and philanthropic community to match his commitment of public dollars.

The city found its first partner in H&R Block. H&R Block has donated \$1 million toward the credit, all of which will go to payments to eligible families. The Mayor's Office worked closely with H&R Block to ensure that their tax preparation services would benefit credit applicants and help them to build assets. As part of the collaboration, H&R Block is offering discounts on tax preparation (\$30 for credit eligible families), is waiving account and Express IRA set-up fees,² and is ceasing to market Refund Anticipation Loans (RALs) in San Francisco.

The Working Families Credit builds on other efforts to raise the visibility of the EITC and to build assets among low-income San Franciscans. The United Way of the Bay Area has marketed the credit as part of its Earn It! Keep It! Save It! campaign. At Volunteer Income Tax Assistance (VITA) sites, tax preparation volunteers provide information about the credit, talk about the disadvantages of RALs, and encourage customers to open bank accounts so that they can receive their federal refund through direct deposit.

Wells Fargo contributes significantly to this initiative by providing staff "on-site" at selected VITA and H&R Block locations and by offering low-cost checking and savings accounts. It also waives ChexSystems³ and instead considers applicants on an individual basis. To help customers build links between their bank account and their savings goals, the Earned Assets Resources Network (EARN), a San Francisco-based IDA provider, distributes information about free financial literacy classes and how to join an IDA program.

Anne Stuhldreher, a Senior Research Fellow at the New America Foundation who helped design the Working Families Credit, says that tax time offers a unique opportunity to help low-income households open bank accounts. "Tax time is the right time to help lower-income families begin to build savings and assets," said Stuhldreher. "These are 'win-win' opportunities for financial institutions to grow new customers and for community groups to help people stabilize their financial lives."

1 During the pilot phase, the amount the Working Families Credit will pay out is dependent on the success of private-sector fundraising efforts.

2 The Express IRA allows clients to open a retirement account with as little as \$300. The initial contribution can be funded from the individual's tax refund. After a client has reached \$1,000 in savings, the client can roll the Express IRA into a more traditional retirement product. About 23,000 account holders have moved their money to retirement vehicles offered by H&R Block Financial Advisors.

3 ChexSystems maintains records of bank customers that have either bounced checks or committed fraud in the last five years. Banks often access ChexSystems when reviewing an application of a new customer for a checking account.

the EITC, they also educate consumers about the disadvantages of Refund Anticipation Loans, which can significantly reduce the size of a family's refund check.

Governmental support can also significantly increase program participation rates. Efforts in the state of Washington, for instance, demonstrate that government outreach can greatly boost the number of EITC filers. In 1998, the IRS estimated that 40 percent of eligible Washingtonians were not applying for the EITC. The state made the decision to spend a modest sum of money—\$316,000—to develop an EITC awareness campaign. The campaign included direct mail, radio, transit and television advertising, public service announcements, internet information, and distribution of posters throughout the state. A toll-free hotline distributed EITC information and forms and referred callers to free tax assistance sites. State employees also contacted nearly 8,000 welfare-to-work clients to make sure that they knew about the EITC. As a result of this effort, an additional 3,667 households in Washington applied for the credit, adding \$29 million in EITC refunds to the local economy in a one-year period.⁴ In an innovative program in San Francisco, Mayor Gavin Newsom is piloting a local tax credit to increase the

number of city residents who claim the EITC (Box 5.1: San Francisco's Working Families Credit).

There is also a growing recognition that the EITC can dovetail with asset building policies and programs. Participants in the United Way of King County's IDA program, for example, can deposit their EITC refund into their IDA account, and receive up to \$1,500 in matching funds. Utah Saves is linking the EITC with a statewide initiative to encourage savings and retire debt. The goal is to reduce the rate of personal bankruptcy filings in Utah—the highest in the nation—by providing low-cost bank accounts and financial education.

Given that federal refunds to low-income families total approximately \$30 billion,⁵ the potential for leveraging the credit for asset building is substantial. The EITC successfully lifts millions of families out of poverty each year; the goal now is to expand efforts to help those millions of families use the EITC to build wealth and invest in their future.

For a list of resources on the EITC, as well as information on how to volunteer or host a free tax preparation site for next year, please visit www.pointsoflight.org/programs/eitc/facts.cfm. 

COMMUNITY INVESTMENTS



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Endnotes

Savings In The Spotlight

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- ⁸ Lillian Woo, F. William Schweke, and David Buchholz (2004). *Hidden in Plain Sight: A Look at the \$335 Billion Federal Asset-building Budget*, Washington, D.C.: Corporation for Enterprise Development.
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- ¹¹ Comptroller of the Currency (2005). "Individual Development Accounts: An Asset Building Product for Lower-Income Consumers," *Community Development Insights*, February 2005. Ellen Seidman and Jennifer Tescher (2004). *From Unbanked to Homeowner: Improving the Supply of Financial Services for Low-Income, Low-Asset Customers*, paper prepared for the Joint Center for Housing Studies, Harvard University.
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- ¹⁴ Ibid.
- ¹⁵ Robert Kuttner (2003). "Sharing American's Wealth: The Policies and Politics of Building a Larger Middle Class," *The American Prospect*, Volume 14, Issue 5.
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- ¹⁹ Federal Reserve Bank of Cleveland (2004). "Individual Development Accounts: An Endangered Wealth-Creation Strategy?" *Community Reinvestment Forum*, Winter 2004.
- ²⁰ For example, income guidelines for AFIA grants are 200% of the poverty level, while grants from the Federal Home Loan Bank IDEA program are directed at households who make less than 80% of area median income.
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- ²⁷ For the most recent updates on federal asset building legislation, visit the Policy link at www.assetbuilding.org.
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Individual Development Accounts

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The Asset Policy Initiative of California

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