



Jacob Bastian on the Real Costs of the EITC

November 2018 podcast episode transcript

Jacob Bastian, Postdoctoral Scholar, University of Chicago Harris School of Public Policy

Hosted by Dave Chancellor

Chancellor Hello and thanks for joining us for the Poverty Research and Policy Podcast from the Institute for Research on Poverty at the University of Wisconsin-Madison. I'm Dave Chancellor. For this, our November 2018 episode, we're going to be hearing from Jacob Bastian about the real public costs of the Earned Income Tax Credit. I was able to talk to Bastian, who is a postdoc at the University of Chicago Harris School, when he visited Madison this fall to speak at the Public Economics Seminar Series hosted by UW's economics department. To start off, I asked him to give us a quick primer on what the Earned Income Tax Credit or EITC is and how it works.

Bastian The Earned Income Tax Credit is one of the most important parts of the U.S. social safety net today. This program is about a \$65 billion dollar program. It helps about 27 million families per year. It's like a wage subsidy. If you are a working family and let's say you work, you earn \$8 an hour, close to the minimum wage, at the end of the year, you file your taxes and then you basically get money back. So instead of paying taxes, this is a program that gives you money back. If you're a family earning \$8 an hour and you have one child, then when you file your taxes, you're actually going to get about \$3,500 back. If you have two kids, you might get about \$5,500 back. And if you have three kids, you might get \$6,500 back. The way the EITC works is it supplements the earnings of low-income families and it depends on how many kids you have, if you're married or not. This is one of the largest programs in the U.S. today that's helping working low-income families.

Chancellor Bastian says that even just a few years ago, the data for the research questions he's asking about the EITC didn't really exist. So I asked him to talk more about what this data is and the partnership that allowed him access to it.

Bastian This is a project with Maggie Jones, who works at the U.S. Census. And what we have, to get into the weeds a little bit, we have linked administrative data. So what that means is that we have Current Population Survey data, which is survey data, it has interesting information like, how much education do people have? how old are they? And we can link this to tax data. Tax data is fantastic because it's completely anonymous, but it has information on what people are earning. And so what we can do is we can ask a research question like "does the EITC help pay for itself? And what we can do is we can look at low-income families. We can find that they're more likely to work and we can use information on their actual income and their actual earnings. Because it's well known that in survey data, low-income families underreport their income, they underreport their public assistance they get, and so by using tax data, we can look at how much they're actually getting on their tax returns. Using this data, we can ask the question, 'when the EITC expands, do these families pay more tax revenue, do these families receive less public assistance?'"

Chancellor Bastian says that in theory, the EITC could raise or lower receipt of other forms of public assistance. Although we might expect that someone working more, earning more would receive less public assistance, he says there are scenarios in which working more could increase someone's access to some benefits.

Bastian One way to phrase that is, is the EITC a complement or a substitute with other public assistance programs? So on one hand, if the EITC encourages low income families to work more, that might reduce their eligibility for welfare, for food stamps, and for public assistance, because a lot of times with those programs, for every dollar that a family earns, they might lose 30 cents worth of benefits. However there are other programs like disability and unemployment insurance that actually require a work history. And so if the EITC encourages some mothers to work more, it actually could lead to more disability payments, more unemployment insurance benefits. And so with that in mind, it's theoretically ambiguous whether the overall effect of the EITC is going to increase or decrease public assistance usage. And what we find is that although there are small increases in unemployment and disability, the reductions in welfare, food stamps, public housing, is much larger than that.

Chancellor Given all this, I asked Bastian what they actually found when they measured all of these factors.

Bastian In the analysis, what we find is that the EITC offsets about 60 percent of its own costs. At least 60 percent. So what this means is that the real cost of the EITC is about 40 cents on the dollar. However, if you account for the fact that the EITC improves the health of mothers and children, the EITC improves the outcomes of children, they're more likely to graduate from high school, and work and earn more. The EITC is also decreasing mothers going to jail. So, once you account for all of these effects, the EITC may completely pay for itself and it might be something today that policymakers should consider expanding even more.

Chancellor Bastian says that one of the questions we should ask ourselves with these kinds of results is about the time period that they're actually measuring.

Bastian One thing to think about is, ok, so the EITC helps pay for itself, that's interesting. I'm looking at the last 30 years of data, and so, do these results just reflect the 1990s EITC expansion or are these results relevant for policymakers today? And one thing that we do in the paper is we look at more recent EITC expansions. There was a federal expansion in 2009, there's also been a number of state EITC expansions in the last couple of decades. And so, our results suggest that if we don't just look at average effects, but we look at how these effects vary over time, we see that the most recent EITC expansions have continued to encourage low income mothers to enter into the labor force and to earn more and to pay more taxes and then to receive less welfare benefits.

Chancellor And Bastian says that another advantage of looking at the effects of EITC expansions over a long time period is that it helps them separate the effects of those expansions from those of other policies that were in place at the same time.

Bastian So there's been a lot of evidence showing that the EITC has encouraged a lot of moms to begin working. There's been some recent evidence calling that into question and just saying whether, is it the EITC, or is it actually the big welfare reform that happened in the 1990s? And one way that we try to disentangle the effect of the EITC with welfare reform is we take a look at the years before and after 1999. Before and after the year 2000. And what we find is that, even when we just focus on years after the year 2000, we find that the EITC is still encouraging mothers to work. It's still encouraging these mothers to pay more taxes, receive less public assistance and so this suggests that the result we're finding isn't driven by welfare reform. The EITC still seems to be encouraging mothers to work even after the year 2000 and so that suggests that the most recent expansions have continued to have an effect and that additional expansions today would likely continue to do so as well.

Chancellor And Bastian says that their findings may have implications as we think about the EITC for adults who don't have children or dependents.

Bastian The EITC does have benefits available to families without kids, but they're very, very small. So, the EITC for a family with one kid is worth up to about \$3,500 a year. The EITC for a family with zero children is worth only a few hundred dollars. Even for someone making the minimum wage, there's

Bastian, continued basically zero EITC available. So, one implication of these results and just thinking about the EITC in general is that policymakers should seriously consider increasing the EITC for adults without children. It's pretty well known that the employment rates of young adults are decreasing. It's also relevant that a lot of older adults are not working, so maybe an adult is 55 years old, the kids have moved out of the house and so they're not eligible for the EITC and they're deciding not to work. Either there's not a job available to them or they don't want to work at a minimum wage job and so potentially, by expanding the EITC for older workers, or for all workers without children, this is very likely going to be a way to increase the labor force participation and to decrease poverty for these types of families. And so I think, clearly, a version of an expanded EITC for older workers or for adults without children would be a good idea. And the results in our paper show that if these people did work more that they would help pay for the cost of the EITC. And so, by instituting an EITC for older workers or adults without children, the program would likely still cost much less than the actual sticker price.

Chancellor Bastian says that knowing more about the real costs of the EITC has policy significance because, as he noted at the beginning, federal and state EITCs are large and expensive programs.

Bastian It's very likely that additional EITC expansions today would lead to even further increases in low income mothers working and that they would pay more taxes and the reason that that matters is because maybe a governor today thinking about whether to expand the EITC might think, well, I don't know if we can afford another \$50 million, but, if the cost of the EITC is only 30 or 40 or 50 cents on the dollar, then it might make the decision a little bit easier for them or for their constituents if the price of the EITC is actually much less than the sticker price. And so I think these results have implications for policy today.

Chancellor Thanks to Jacob Bastian for talking with us. To learn more about this work and other research he has done on the Earned Income Tax Credit, visit his webpage on the University of Chicago Harris School website.

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