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Are Workers Paid the EITC Shortchanged on Social Security?

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Growing economic inequality in the United States has intensified debate over how to best improve incomes and retirement security, particularly for modest and low-income people. One way to lift incomes is through higher wages. Another way is by having taxpayers subsidize wages through the Earned Income Tax Credit (EITC). While Conservatives typically oppose efforts to raise the minimum wage, there has been considerable bipartisan support for the EITC, including proposals to expand tax credits available for childless workers.

A federal tax credit for low- and moderate-income working people, the EITC has been widely praised for encouraging work while reducing the number of people in poverty. In 2013, the EITC lifted about 6.2 million people out of poverty including about 3.2 million children, according to the Center on Budget and Policy Priorities.ⁱ In the 2013 tax year, the most recent year for which data are available, more than 27 million working families and individuals received the EITC.

For tax year 2015, working families with children with annual incomes below about \$39,000 to \$53,300 (depending on marital status and the number of dependent children) could receive the federal EITC. Workers with no children and incomes below about \$14,800 (\$20,300 for a married couple) could receive a very small EITC.ⁱⁱ Twenty-six states and the District of Columbia have established their own EITCs to supplement the federal tax credit.

As wages rise, either in the marketplace through shifts in labor supply and demand, or through the minimum wage, so do Social Security payroll taxes. Money that workers receive in EITC, however, does not generate Social Security

payroll taxes. Nor does the EITC count toward Social Security earnings upon which future retirement benefits are based.

To the extent the EITC is substituting for higher wages, a case can be made that it may reduce the worker's Social Security income in old age. Despite its many assets as an anti-poverty program, the EITC could be strengthened if the federal government made a contribution to Social Security's trust fund on recipients' behalf. With about \$75 billion in federal EITC expenditures annually, the additional \$9.3 billion resulting from applying the 12.4% Social Security tax rate also could help Social Security's short- and medium-term finances.

Under the current system, a person whose highest earnings averaged \$15,000 a year over 35 years would end up with about \$10,542 in annual Social Security benefits – the same as a worker averaging \$15,000 wages plus various amounts of EITC. A worker averaging \$20,000 in wages would end up with \$1,600 (15%) more in annual Social Security benefits compared with another with the same total income but instead averaging \$15,000 wages and taking home \$5,000 in EITC. Similarly, someone averaging \$25,000 in wages would end up with \$3,200 (30%) more in Social Security benefits than a counterpart averaging \$15,000 and receiving \$10,000 in EITC.

These are first order estimates. The EITC's potential impact on individuals' Social Security benefits would vary widely depending on the size of subsidies and number of years a worker received them. The impact could be substantial for some. In 2015, for example, the maximum EITC for married people filing jointly was \$3,359 for families with one child, \$5,548 for those with two children, and \$6,242 with more than two children. EITC subsidies phase out as income rises.

TABLE 1

2015 Earned Income Tax Credit Parameters

(Filing status married filing jointly)

	Phase-in rate	Phase-in ends	Maximum credit amount	Phase-out begins	Phase-out rate	Phase-out ends
Childless	7.65%	\$6,580	\$503	\$13,750	7.65%	\$20,330
1 Child	34%	\$9,880	\$3,359	\$23,630	15.98%	\$44,651
2 Children	40%	\$13,870	\$5,548	\$23,630	21.06%	\$49,974
>2 Children	45%	\$13,870	\$6,242	\$23,630	21.06%	\$53,267

Sources: CBPP table, Internal Revenue Code, [26 U.S.C. §32\(b\)](#).

In recent years, there has been bipartisan support to bolster the EITC, particularly for childless workers. Sen. Sherrod Brown (D-OH) and the Center for American Progress recently launched a drive for such an expansion.ⁱⁱⁱ In 2017, several bills have been introduced in Congress that would expand the EITC. House Speaker Paul Ryan (R-WI) also has outlined plans for expansion of the EITC.^{iv} Researchers at the Brookings Institution have suggested raising the minimum wage and redesigning the EITC in tandem.^v The American Action Forum, a center-right policy institute, supports expanding the EITC, arguing that it is far more effective in reducing poverty than raising the minimum wage.^{vi}

The United States not only faces the challenge of expanding economic opportunity and reducing poverty, it also has a large percentage of people who are not financially prepared for old age. About half of American households age 55 and older have no retirement savings (such as in a 401(k) plan or an IRA), and about 29 percent have neither retirement savings nor a traditional pension plan, according to the U.S. Government Accountability Office.^{vii}

Perhaps recognizing that many Americans, particularly those with low lifetime incomes, rely exclusively on Social Security for retirement income, the Bipartisan Policy Center recently recommended raising Social Security benefits for lower-income workers as part of a comprehensive plan to improve retirement security.^{viii} Efforts to improve Social Security benefits should include consideration of how the EITC currently impacts retirement benefits for low-to-modest-income people.

Conclusion. The EITC plays a major role in combatting poverty in the United States and there is bipartisan support to expand its role. The EITC’s impact on future Social Security benefits should be further analyzed. Receiving EITC supplements through the tax system instead of higher wages should not result in reduced Social Security benefits for low- and modest-income workers.

ⁱ “Policy Basics: the Earned Income Tax Credit,” Center on Budget and Policy Priorities, Jan. 15, 2016. <http://www.cbpp.org/research/federal-tax/policy-basics-the-earned-income-tax-credit>

ⁱⁱ <https://www.irs.gov/publications/p596/ar02.html>

ⁱⁱⁱ “Get ready for an EITC debate,” Politico, June 7, 2016. <http://www.politico.com/tipsheets/morning-tax/2016/06/get-ready-for-an-eitc-debate-cbo-raises-some-eyebrows-the-pot-wars-214680>

^{iv} “What is Paul Ryan's plan to expand the EITC?,” VOX, Oct. 8, 2015. <http://www.vox.com/cards/paul-ryan-poverty/what-is-paul-ryans-plan-to-expand-the-eitc>

^v “Raising the Minimum Wage and Redesigning the EITC,” Brookings Institution, Jan. 30, 2014. <https://www.brookings.edu/research/raising-the-minimum-wage-and-redesigning-the-eitc/>

^{vi} “Primer: Earned Income Tax Credit and the Minimum Wage,” American Action Forum, Feb. 5, 2014. <https://www.americanactionforum.org/research/primer-earned-income-tax-credit-and-the-minimum-wage/>

^{vii} “Retirement Security: Most Households Approaching Retirement Have Low Savings,” GAO-15-419, May 12, 2015. <http://www.gao.gov/products/GAO-15-419>

^{viii} “Securing Our Financial Future: Report of the Commission on Retirement Security and Personal Savings,” Bipartisan Policy Center, June 2016. <http://bipartisanpolicy.org/library/retirement-security/>
