Enact refundable child tax credit

Tax Type: Individual Income Tax
Origins: Legislation co-introduced by Councilmembers Parker, Mendelson, Allen, Henderson, Lewis-George, Nadeau, Pinto, R. White, and T. White. A CTC was also recommended by the Fair Budget Coalition.
Commission Goal: Progressivity and racial equity

Current Law
The District does not offer a child tax credit (CTC). Fourteen states currently offer a CTC, including 11 that provide a refundable credit.

Proposed Change
Councilmember Parker's proposal would provide a fully refundable $500 child tax credit for up to three eligible children younger than age 17.[1] The credit would phase out between $100,000 and $125,000 in adjusted gross income (AGI) for single filers and $145,000 and $175,000 for married filers.

The TRC staff also analyzed two other CTC options:

1. A $500 refundable CTC available to children younger than age 6 with a 5 percent phaseout rate beginning at $30,000 for single filers and $60,000 for married files.
2. A $500 refundable CTC available to children younger than age 17 with a 5 percent phaseout rate beginning at $200,000 single filers and and $400,000 for married filers.

These alternative proposals were put forward as extremes—restrictive eligibility and broad eligibility—to illuminate the options available to policymakers when designing a CTC. There is no cap on the number of eligible children per household for these two proposals.

The Commission could also recommend the District deliver its CTC to eligible families in *advanced* monthly or quarterly installments. Minnesota recently became the first state to approve advanced payments of its CTC, but its Department of Revenue is still working on an implementation plan.

Arguments for Change
- *Supports children.* Children in low-income families that receive the federal CTC (and EITC) do better in school, are more likely to attend college, earn more as adults, and are healthier. Fully 97 percent of households with incomes below $35,000 that received the federal CTC reported using the money to pay for basic needs like food, clothing, rent, and utilities.

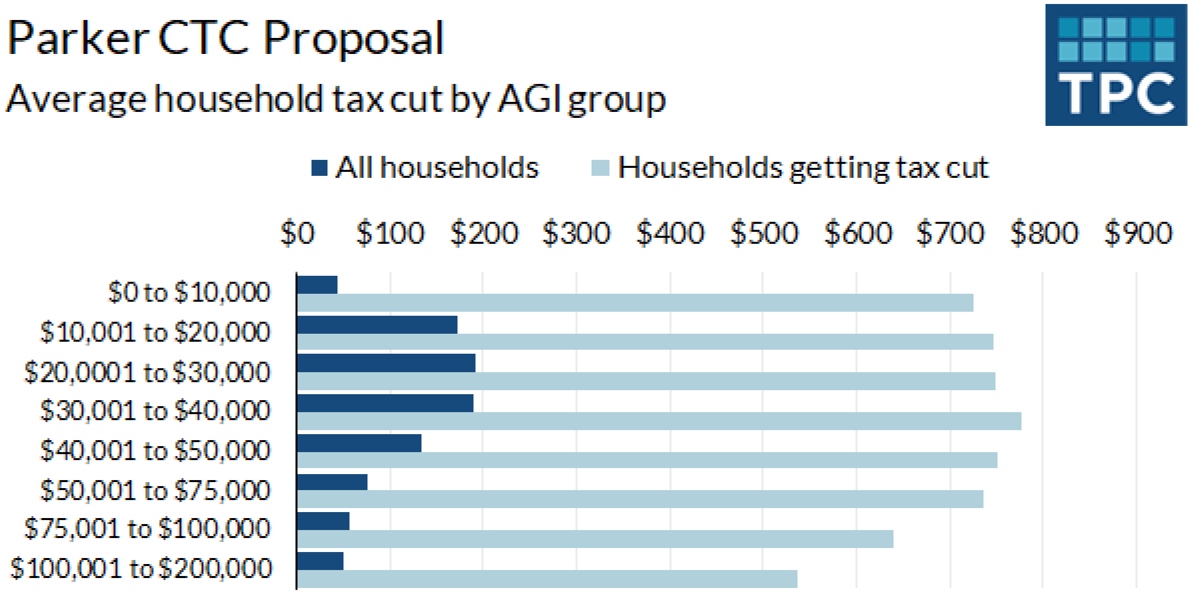
[1] CM Parker's initial proposal was for children younger than age 17 (the same as the federal CTC). A later proposal, put forward during budget negotiations, limited the CTC to children younger than age 12. We are analyzing the original proposal for children younger than age 17.

- *Mitigates poverty.* Despite a recent decline, child poverty remains higher in the District (17 percent in 2022) than the national average (17 percent). (These figures reflect the Census Bureau's official poverty measure, which excludes the impact of tax credits and noncash benefits like SNAP as well as geographical differences in cost of living.) The COVID expansion of the federal CTC lifted or eased poverty for 25,000 children in the District.
- *Targets benefits at difficult to reach parents.* Households with low or no income are *not* eligible for the federal and DC EITC because the credit requires a minimum amount of earned income to qualify. The DC CTC, not based on earned income, could fill a gap of government support.
- *Supports more children than similar programs.* A child tax credit could also benefit children living in middle-income households, a group that also largely does not benefit from the federal or DC EITC. (Households with roughly $50,000 or more in AGI earn too much to benefit from the EITC.) The Parker proposal, available to families earning up to $175,000, would benefit more than two-thirds of DC children. The broader eligibility CTC would reach even more DC children.
- *Provides a level of basic income (monthly or quarterly payments)*. There is evidence that the federal government's monthly CTC payments—provided for one year as part of the American Rescue Plan—helped families catch up with past due bills and pay regular expenses such as rent and utilities. There is also evidence that a plurality of families preferred receiving the CTC in advanced monthly payments rather than as part of their tax rebate.

Arguments against Change

- *Many families with children already benefit from the District's EITC.* The District's EITC already reaches an estimated 56,000 children in the District. The District's EITC (it will match 100 percent of the federal EITC by 2025) is the most generous state EITC in the country.
- *Simplicity and administrative challenges (monthly or quarterly payments)*. Providing a CTC in monthly or quarterly payments could confuse filers who typically receive tax credits as part of their once-a-year tax rebate. Further, providing *advanced* payments (in contrast to *delayed* payments, as part of the DC EITC) could result in DC OTR needing to reclaim mispaid benefits.
- *Possibly disrupt SNAP benefits (monthly or quarterly payments)*. Supplemental Nutrition Assistance Program (SNAP, i.e., food stamps) regulations do *not* count lump-sum refunds as part of income when calculating benefits. However, the regulations are not clear on distributing benefits in monthly or quarterly payments. Thus, delivering them this way could possibly result in lowering recipients' SNAP benefits. Minnesota, the first state to approve quarterly CTC benefits, is still figuring out the administrative part of their enacted legislation.

Distributional Analysis from TPC State Tax Model



Source: TPC state tax model.
Note: The CTC delivers a tax cut to 12% of DC households. These households get a significant tax cut, but most households do not get a tax cut. No households earning above $200,000 get a tax cut.

Among all DC households, the Parker CTC proposal provides an average annual tax cut of $85, with the largest average tax cuts concentrated among households earning $10,000 to $40,000. However, the CTC is only available to DC households with children, and thus only 12 percent of DC households benefit from the tax cut. Among those 12 percent of households benefiting from the CTC, the average annual tax cut is $710, with benefits relatively equal among income groups until the credit is phased out at higher incomes. The reason the average tax cut is larger among those earning $10,000 to $40,000, when looking at all DC households, is because households at those income levels are more likely to have children (roughly 25 percent for each group) than higher-income DC households (roughly 10 percent for those earning $50,000 to $100,000). Thus, while all eligible households receive a similar tax cut, the overall benefits of the Parker CTC are concentrated among lower-income households because of family characteristics. (Note: Households earning less than $10,000 are eligible for all three CTC proposals, but they see smaller average tax cuts because households with this level of income are less likely to have children than households earning above that level.[2])

The restrictive CTC proposal only benefits 4 percent of DC households, both because it excludes households earning above the income limits and because only children younger than age 6 are eligible. For example, even among the income groups targeted by the more restrictive credit, households earning

[2] Households with no or little earnings would be eligible for the CTC under these proposals. However, some of these households might not currently file income tax because they do not have a liability and do not receive benefits like the EITC. Thus, the District might need to actively recruit these households to file tax and receive the benefit, similar to [federal and state implementation efforts] related to delivering the 2021 expanded federal CTC.

$10,000 to $50,000, fewer households get the restrictive CTC than under the other two proposals because some of these households only have children ages 6 and older. Most states restrict income eligibility or age eligibility so they can either A) provide a bigger credit amount and thus concentrate benefits on these groups or B) limit revenue loss. On the former, for example, Oregon recently enacted a CTC similar to the restrictive proposal outlined here, but Oregon's CTC is a $1,000 credit. We kept credit amounts the same in our proposals to show how these policy levers affect the distribution of benefits.

The broad CTC proposal had benefits similar to the Parker proposal but provided more households (14 percent of DC households) a benefit because it has higher income phaseouts. (The three child maximum in the Parker proposal does not affect many households. If we cap the broad CTC proposal at three children there is only $1 million saved in revenue cost.) Specifically, under the Parker proposal, 9 percent of households earning between $100,000 and $200,000 benefit and no households earning above $200,000 benefit. Under the broad CTC proposal, 13 percent of households earning between $100,000 and $200,000 benefit and 18 percent of households earning between $200,000 and $500,000 benefit.

	DC households w/ tax cut	DC households w/ tax cut $10-$50,000	DC households w/ tax cut $50-$100,000	DC households w/ tax cut $100-$500,000	Avg tax cut eligible households
Parker CTC	12%	18%-26%	9%-10%	0%-9%	$710
Restrictive CTC	4%	12%-14%	0%-2%	0%	$575
Broad CTC	14%	18%-26%	9%-10%	13%-18%	$746

Racial Equity Impact

A refundable tax credit targeted to children would advance progress toward racial equity. The District's children as a whole are disproportionately Black and Hispanic; some 52 percent are Black and 17 percent are Hispanic, while 24 percent are white. Because of a long legacy of racial inequity in employment and wages, access to education, and pathways to building wealth, the proportion of children who are Black and Hispanic is particularly high among families with lower incomes. For example, DC families with incomes below 300 percent of the federal poverty line—the group targeted by the DCFPI proposal—represent 71 percent of Black children, 45 percent of Hispanic children, 35 percent of Asian-American and Pacific Islander children, and 5 percent of white children. So income targeting would increase the extent to which the credit benefits children of color. Generally speaking, the tighter the income targeting, the more the credit would do to advance racial equity.

Revenue Estimate

According to ORA, Councilmember Parker's CTC—in the version that applied to children under 12—would cost $19.1 million in FY 2025. ORA did not provide a revenue estimate for the Parker proposal providing a CTC for children younger than age 17.

Enact a Refundable Child Tax Credit ($millions)

	FY 2025	FY 2026	FY 2027
Councilmember Parker's CTC (children under 12)	-13.1	-19.2	-19.3

Source: ORA

The Tax Policy Center state tax model estimated the annual cost of all three CTC options (for children under 17):

1. Parker's CTC: $39 million
2. Restrictive CTC: $9 million
3. Broad CTC: $47 million

Further Reading

1. "State Child Tax Credits and Child Poverty: A 50-State Analysis," ITEP, 2022.
2. "Narrowing the Racial Wealth Gap Using the EITC and CTC," Brookings, 2022.
3. "Many Adults with Lower Income Prefer Monthly Child Tax Credit Payments," Urban Institute, 2022.
4. "Families Planned to Use Child Tax Credit to Pay Bills but Some Were Confused About Eligibility," Tax Policy Center, Urban Institute.
5. "Minnesota Previews Implementation Plan for New Child Tax Credit," *Tax Notes*, August, 2023.