

# Strengthening and Modernizing the California EITC to Fight Child Poverty, Inequality, and the Rising Cost of Living

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## SUMMARY

This memo explores a Cost-of-Living Refund to put cash into working Californians' pockets by modernizing and expanding the state's Earned Income Tax Credit (CalEITC).

*Building upon the existing CalEITC, this policy will:*

- Reduce poverty and child poverty and use the proven benefits of cash transfers to boost a range of educational and health outcomes for California children.
  - Help working and middle-class people face the rising cost of living and housing, with a leg up out of poverty or a cushion of financial stability.
  - Fight rising inequality that plagues the state and threatens our democracy.
  - Make taxes fairer, reducing the high share of taxes paid by low-income people across California.
  - Build on our high minimum wage, so workers earn enough to live.
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# THE COST OF LIVING AND HOUSING RISING ALONG WITH INEQUALITY

The steep and rising cost of living and housing, coupled with stagnating incomes, means too many families cannot take part in the American promise: If you work hard, you can get ahead in our country. Many people live on the financial brink, as the cost of middle-class life has dramatically increased—from housing to childcare to medical costs—while wages lag behind.

At the same time, income inequality is at a peak, and is worse in California than in most other states. While millions of low-wage workers—predominantly people of color—struggle to make ends meet, in the words of a working-class voter, “The rich are getting richer while everyone else is stuck.” The tax code exacerbates this problem: Even in California, low-income people pay more of their income in state and local taxes than most other taxpayers (per [ITEP data](#)).

As a simple and effective approach to fight rising economic inequality and financial instability, we need to put more money back in the pockets of the working and middle-class people who need it most.

# PUTTING MONEY BACK IN WORKING PEOPLE’S POCKETS

A Cost-of-Living Refund, or Working Families Tax Credit, established by modernizing and expanding on the important and incremental benefits of CalEITC, is a powerful and practical plan to provide relief to low-income and middle-class people.

On the merits, there is no simpler or better-tested policy to provide economic stability to working and middle-class people. The federal EITC already lifts more families out of poverty than food stamps, housing subsidies, and unemployment insurance combined, because cash gives people the tools to solve their own problems. Today, 57% of Americans don’t have enough cash on hand to cover a \$500 unforeseen expense, with significantly worse rates among people of color.

Yet, in its current form, the CalEITC cannot fully address the needs of hard-working families in an economy shaped by low-wage work and high concentrations of wealth.

The Cost-of-Living Refund builds on the CalEITC to reduce the poverty rate substantially and create a foundation for economic mobility:

- **Benefits nearly half the population.** This policy is designed to benefit 40% of all California residents, including a majority of the state's children.
- **Makes a simple promise to voters.** "If you work and you earn less than \$75,000, you get a Cost-of-Living Refund of \$1,200 extra cash a year, and if you have kids, you get more."
- **Addresses the racial wealth and income gap.** About three-quarters of the recipients of an expanded EITC are [people of color](#), beginning to nudge in the direction of repairing hundreds of years of policies creating poverty disproportionately in communities of color.
- **Reaches low-income and middle-class families to reduce poverty.** The poorest people and families with children benefit the most under this plan, significantly reducing child poverty, while also supporting people in the middle class who desperately need financial stability. Because communities of color and rural residents live in higher levels of poverty, it provides a significant boost to these communities.
- **Excites voters seeking new economic solutions.** A framework that resonates with the public, this [policy polls well](#), and remains popular with voters even after negative arguments. It is particularly popular with less-likely voters, giving them an additional reason to turn out.
- **Complements \$15 minimum wage.** The minimum wage sets a floor that pushes back against potential wage decline, and thus couples well with the many positive aspects of the EITC.
- **Provides a pro-worker and pro-family policy that is a bold response to federal tax cuts.** Addresses the tax cuts that dramatically benefit the wealthy, restoring the share of taxes paid by top earners and cutting taxes for working people who are hit harder by sales and gas taxes.
- **Offers a progressive answer to future of work questions.** With 40% of workers now in the gig economy, part-time jobs, or other contingent work, it's important that those with precarious work lives have financial stability. A Cost-of-Living Refund can also soften the blow of the transition caused by the impact of automation and artificial intelligence on American jobs, or help workers afford time to gain new skills.

Alongside affordable health care, higher wages, better working conditions, high-quality public education, and robust public services, a guaranteed income that puts cash in the pocket of hard-working Americans every month and stabilizes families' economic lives is a critical part of helping people make their way in this economy and beginning to address the racial wealth gap.

# TAX CREDIT POLICY DETAILS

The goal of the Cost-of-Living Refund is to provide a meaningful income boost that reaches up into the middle class, to help Californians who are working (including those whose work is unpaid caregiving or attending school) while struggling to keep up with the state's rising cost of living. Policy details can be modified to target the total cost and who benefits, as shown in these three policy pathways below (and those pathways, and their component parts, can be further disaggregated in terms of costs of specific expansion opportunities and who benefits, as needed):

	Starting Refund	Medium Refund	Full Cost-of-Living Refund
Reach	Reaches <b>29% of CA residents</b> (10.7M recipients) and <b>40% of children</b> (4.4M child recipients).	Reaches <b>38% of CA residents</b> (14.3M recipients) and <b>51% of children</b> (5.6M child recipients).	Reaches <b>40% of CA residents</b> (15.1M recipients) and <b>54% of children</b> (5.9M child recipients).
Coverage	<b>Covers people earning up to \$50,000</b> (or level of federal EITC, whichever is higher). 9% of those in the middle income quintile receive a credit.	<b>Covers people earning up to \$50,000</b> (or level of federal EITC, whichever is higher). 9% of those in the middle income quintile receive a credit.	<b>Covers people earning up to \$75,000</b> . 33% of those in the middle-income quintile receive a credit.
Credit amount	<b>25% match</b> of federal EITC, <b>plus a basic credit of \$1000</b> a year (the minimum amount for recipients not on phase-in or phase-out), and includes family caregivers.	<b>30% match</b> of federal EITC, <b>plus a basic credit of \$1,000</b> a year, and includes family caregivers and low-income students.	<b>50% match</b> of federal EITC, <b>plus a basic credit of \$1,200 a year</b> , and includes family caregivers and low-income students.
Amounts for Families	Families with three or more children receive about <b>\$1611</b> .	Families with three or more children receive about <b>\$1930</b> .	Families with three or more children receive about <b>\$3,200</b> .
Average Tax Credit	Average tax credit is <b>\$852</b> for those receiving credit in bottom income quintile.	Average tax credit is <b>\$986</b> for those receiving credit in bottom income quintile.	Average tax credit is <b>\$1,368</b> for those receiving credit in bottom income quintile.
Revenue	New revenue required is estimated at <b>\$3.47 billion</b> .	New revenue required is estimated at <b>\$5.12 billion</b> .	New revenue required is estimated at <b>\$7.88 billion</b> .

All three policy pathways have the following components:

	Starting Refund	Medium Refund	Full Cost-of-Living Refund
CalEITC	Increase the amount of current CalEITC to provide a much more generous credit than the few hundred dollars many recipients get under the current policy.		
Definition of Work	Expand the definition of work to include unpaid family caregivers. The Medium and Full Cost-of-Living Refunds also include students.		
Monthly Benefit	Create an option to receive the benefit monthly so people feel it working in their lives.		
Fairness	On the heels of federal tax cuts on the wealthy, we can pay for this expansion by increasing taxes on those who've done well in the new economy, to make taxes more fair.		
Equity	Based on analysis by California Budget & Policy Center of an earlier version of the policy going up to \$50K of income, 72% of recipients would be people of color (compared to 66% of taxpayers).		
Poverty	Child poverty would be cut by 13% and overall poverty would be cut by 10%.		

## BUILDING ON POLICY OPPORTUNITIES

Since the CalEITC was established in 2015, the state has continually invested in and expanded eligibility for the credit. The Cost-of-Living Refund builds on this momentum and paves a pathway for creating boosts to savings and wealth-building for low-income families.

The policy offers the opportunity not only to lift families out of poverty, but also to increase savings opportunities for low-income families. Being able to save for immediate, short-term, and long-term goals is imperative for families in weathering a financial storm and in achieving prosperity. In California, 54% of households report not having saved for emergencies in the past 12 months. Thirty-seven percent of families do not have three months of savings to live above the federal poverty level should they have a disruption in income. When it comes to long-term savings for goals like retirement, college education, or homeownership, Californians also struggle. For example, over half of private sector employees in California work for an employer that does not offer a retirement account.

CalSavers was authorized in 2016 to address this issue by automatically opening a Roth IRA for all employees not currently offered a retirement plan through their employer. The Cost-of-Living Refund could provide additional income for workers to save when CalSavers rolls out in 2019.

The Cost-of-Living Refund could also pair well with something like a statewide children's savings account (CSA) program. For example, the state could offer a match for low-income families that decide to use a portion of their refund to save in a children's savings account. This opens the opportunity for the Cost-of-Living Refund to transform over time from a support for short-term uses into a small seed for families' long-term savings goals.

Other policy opportunities include: (1) extending the Cost-of-Living Refund to [ITIN filers](#) (taxpayers who don't have a Social Security number) so that all work is acknowledged; and (2) exploring ways to make it easier to claim the credit, so that workers who are not required to file tax returns (because nothing is owed) actually receive the credits they have earned.