



Periodic EITC Payments

Recommendations for Federal Credit

February 2019

Monthly payment of the EITC helps make ends meet. Instead of waiting until tax time, families can receive distributions throughout the year, raising their income in real time.

OVERVIEW

As the cost of living rises and working and middle class families struggle, attention is focusing on ways to modernize the Earned Income Tax Credit. Some are proposing innovative ideas to get cash into working Americans' wallets as needs arise. ESP advocates for monthly payment of the EITC to better help families make ends meet. Instead of waiting months to receive their EITC at tax time, families would receive distributions throughout the year, raising their income in real time.

After deciding to pursue periodic payment of the EITC, policymakers will face several additional policy and implementation questions that will need to be resolved before the program can be launched. This memo summarizes some of the most important questions to consider.

KEY POLICY QUESTIONS AND RECOMMENDATIONS:

1. *Should the program provide real-time disbursement or delayed payment?*

Disbursing the EITC during the tax year in which taxpayers are entitled to receive it helps families when they actually need funds, but requires advance prediction of annual income to determine eligibility. Delayed payment does not require prediction, but does not respond to financial needs as they arise.

Recommendation: Provide real-time EITC payment, not deferred receipt, but provide a safe harbor provision. Real-time payments provide help when it's needed. But to ensure that good faith claimants aren't dramatically penalized for an unexpected change in circumstances such as getting a mid-year raise, consider providing safe harbor for some amount of overpayment, e.g. a minimum safe harbor of \$250. The popularity of the ACA advance premium tax credits, which can result in overpayment at the end of the year, indicate that the existence of some overpayment in a program is not a fatal flaw.

2. *Who should be eligible for periodic payments?*

While policymakers may want to allow anyone who believes they will be eligible for periodic payments to receive them, there is some risk of overpayments, particularly to those unfamiliar with the EITC. Restricting eligibility to filers who have been eligible in the past reduces this

problem, but excludes otherwise eligible needy recipients. (This is not a problem for delayed payment.)

Recommendation: Make periodic payments available to all EITC recipients. To reach the largest population possible of those in need, periodic payments should be available to all recipients. A more limited (and complex) approach would be to restrict eligibility initially to those who have received the EITC previously in the past two years.

3. *What agency should administer payments?*

The IRS administers the EITC currently and is best positioned to determine eligibility. The IRS could process periodic payments, with sufficient resources for administration and implementation, or could delegate the payments to the U.S. Department of the Treasury, Financial Management Service, which makes payments of other federal benefits on the Treasury Direct Express Card.

Recommendation: Allow IRS to decide how to implement the payments, while providing sufficient funding for administration.

4. *How should payments be distributed?*

Payments could be offered by debit card, direct deposit, check, or added to paychecks by adjusting withholding.

Recommendation: Mandate electronic payments, by direct deposit or debit cards only.

Check cashing and predatory loan companies prey on needy Americans, and payments by check increase their opportunity to do so. Dispersal through a paycheck line item may go unnoticed and burdens employers with administering a program. Paying by direct deposit or debit cards ensures that those who need these payments actually recognize and receive them, provided that debit cards do not charge significant fees.

6. *Should periodic payments be made monthly or quarterly?*

Monthly payments provide more consistent assistance and additional flexibility, but quarterly payments provide larger sums.

Recommendation: Make periodic payments monthly. Monthly payment makes sense for the simple reason that a significant portion of expenses for low- and middle-income families are monthly or more frequent (e.g., rent, child care, utility bills). Monthly payments also give recipients the flexibility to save a small amount at a time and build up a savings cushion.

5. *Should monthly payments be optional or mandatory for the recipient?*

A universal system of monthly payments may be simpler to administer. However, EITC filers accustomed to receiving a lump sum may be surprised not to receive it. Making the monthly payments optional gives recipients the ability to choose which mode is better for them.

Recommendation: Make monthly payments optional for the recipient. Surveys have found that about half of respondents would initially prefer a periodic payment to receive help in real time, and half would rather receive a lump-sum payment that some find preferable for savings. Some studies have also found that filers are very satisfied with periodic payments once they receive them. Data from behavioral economics suggests that the best mechanism

for this selection is a simple forced choice (with no default option) between monthly payments and a lump sum payment. A middle option could also be added, for “half of your refund in periodic payments and the other half in a lump sum.” (In the case of an advance credit, clearly a worker needs to be able to claim a lump sum credit the next year if they don’t file for an advance.)

7. *Should periodic payments be available to all EITC recipients?*

A range of recipients may prefer monthly payments, but some may be eligible only for small amounts.

Recommendation: Make periodic payments worth electing. Some participants in prior studies on periodic payments found them unhelpful when the payments were too small. Consider extending eligibility for periodic payments only to those who will be entitled to at least \$20 per month. If monthly periodic payments would be too low to make a meaningful difference for many recipients, consider allowing taxpayers to elect quarterly payments instead.

8. *Will monthly payments affect other safety net programs?*

Generally, tax refunds are not treated as income for the purposes of eligibility for other programs. However, federal law is ambiguous on this topic as it relates to periodic payments.

Recommendation: Periodic payments should clearly not count as income. Just as lump-sum tax refunds are not treated as income by other federal benefit programs, choosing periodic payments should not penalize recipients of other government aid.

ADDITIONAL CONSIDERATIONS FOR IMPLEMENTATION:

Policymakers should engage in early conversations with the agencies who will oversee periodic payments to ensure that they are prepared for implementation, and can provide information about their existing limitations that will need to be mitigated.

Consider asking:

1. For real-time distribution, when will the agency need filers to predict the year’s income?
2. What process will the agency set up to allow filers to update their income and eligibility for the credit throughout the year, or to change their direct deposit information?
3. How will the agency develop a method for reconciliation of possible overpayments on the year’s tax return?
4. What will the costs of administering a periodic payment program be?