



Do Single Mothers Use the Earned Income Tax Credit to Reduce Unsecured Debt?

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Acknowledgements

- Research published in *Review of Economics of the Household*, with Xiaoqing Song and Trina R. Williams Shanks.
- Work supported in part by a grant to Shaefer from the National Poverty Center, supported by award #1 UO1AE000002-02, from the US Department of Health and Human Services, office of the Assistant Secretary for Planning and Evaluation, and in part by a grant from the National Science Foundation, award No. SES1131500.
- Opinions expressed are the authors' alone.
- Thanks to Jennifer Romich, Sheldon Danziger, and two anonymous reviewers for helpful comments

Background

- ❑ The Earned Income Tax Credit (EITC) is a refundable tax credit for low-income workers, mainly targeting families with children
- ❑ It provides a large income transfer based on the household's (tax filing unit) earnings from the previous year
- ❑ Single mother households make up a majority of EITC recipients

Study Questions:

- ❑ How do they use this unrestricted income transfer?
- ❑ Do they use part of it to reduce unsecured debt?

Background II

- EITC began as a tiny program in the 1970s, but had grown to \$54 billion in federal expenditures in 2012
 - 2012 federal expenditures on TANF were \$17 billion
 - More than 20 states have their own, supplemental, EITC
- The EITC schedule is novel:
 - The credit increases with earnings, up to a plateau, and then phases out slowly, reaching zero at about 200% of poverty
- We are not talking chump change. 2012 max credit:
 - \$6,044 for a family with three children
 - \$5,372 for a family with two children
- The credit is delivered as an unrestricted, lump sum income transfer at tax time
- Unlike any other means-tested benefit we provide

Background III

Existing research suggests recipients spend their EITC on:

- ❑ Paying bills and other making-ends-meet expenses
- ❑ Future investments: Savings/big purchases like a car
- ❑ Current consumption

This Research Suggests:

- ❑ EITC should have an ambiguous effect on secured debt
 - May pay off secured debt, or use the EITC to take on more
- ❑ But should have an unambiguous, negative effect on unsecured debt
- ❑ The past few decades have seen an explosion of unsecured debt, which can often be deleterious to low-income households

The EITC's BIG BANG

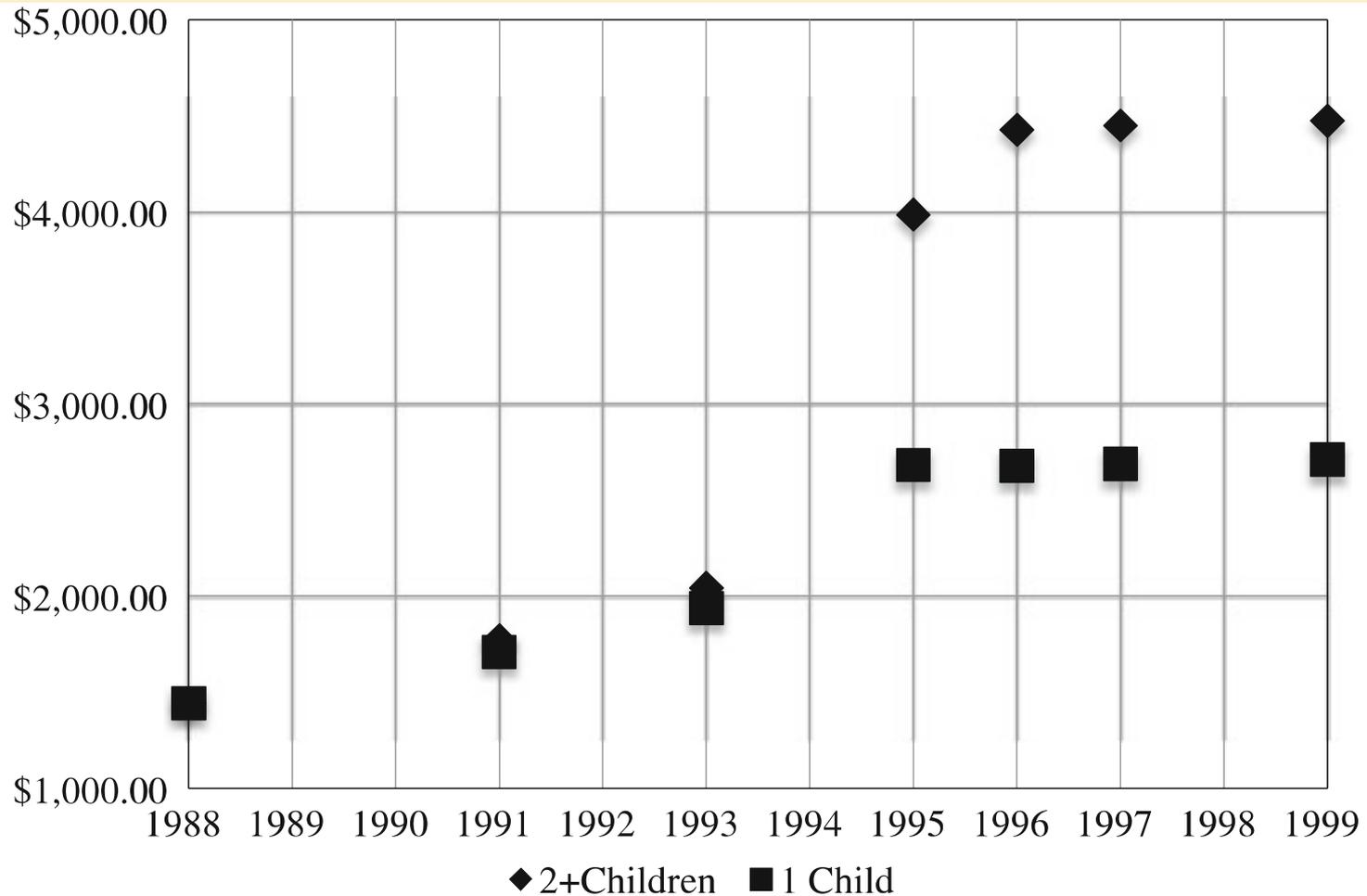


Fig. 1 Maximum EITC benefit per tax year. Source: Tax Policy Center. <http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?Docid=36>

Current Study: EXPLOITS THE BIG Bang

- Assess whether the EITC expansions were associated with reduced unsecured debt of recipients
- Focus on single mother households, who make up a majority of EITC recipients
- Examine unsecured debt by year (adjusted for inflation) over the study period, 1988 - 1999
- Make two difference-in-differences comparisons:
 - Compare single mothers to single childless women
 - Compare single mothers with 2+ kids to those with 1 kid (because those with 2+ got a bigger shock)

The Survey Of income and Program Participation

- ❑ Nationally representative, longitudinal household survey administered by Census
- ❑ 2-4 year panels
- ❑ Data collected every 4 months on all household members
- ❑ Relatively good at capturing income among the poor and public program participation (low rates of under-reporting) Czajka et al., 2003
- ❑ Includes modules on asset and liabilities, which do a (relatively) good job of capturing wealth among low-income households
- ❑ **Unsecured debt:** credit card, store bills, unsecured loans, money owed individuals, and other debts

Method

- ❑ Looking over the period of the EITC increase, compare the unsecured debt of single mothers relative to that of single childless women
- ❑ Then compare the unsecured debt of single mothers by number of children
- ❑ Unsecured debt of the experimental group should fall relative to the control group following the EITC shocks

Results

| | | | | |
|-----------|--------------|--------------|--------------|--------------|
| (0.025) | (919.5) | (1,129.6) | (533.6) | (475.6) |
| 0.005 | -408.05 | -530.28 | 969.04 | -488.16 |
| (0.020) | (600.2) | (486.3) | (784.2) | (454.7) |
| -0.024 | -801.03 | -186.52 | -346.76 | -1,105.41** |
| (0.016) | (657.8) | (719.9) | (477.8) | (496.5) |
| -0.026 | -2,631.25*** | -3,132.00*** | -2,189.69 | -2,193.74*** |
| (0.019) | (580.9) | (1,019.3) | (1,326.2) | (443.7) |
| -0.017 | -1,552.47*** | -1,589.48*** | -788.04* | -1,927.63*** |
| (0.022) | (464.2) | (490.4) | (412.1) | (449.7) |
| -0.001 | -2,266.85*** | -1,632.70*** | -527.56 | -2,009.38*** |
| (0.025) | (685.1) | (547.8) | (490.19) | (458.5) |
| - | - | - | - | - |
| -0.130*** | -1,605.22*** | -1,400.14*** | -1,753.87*** | -1,623.55*** |
| (0.011) | (202.3) | (265.5) | (251.3) | (115.6) |
| -0.101*** | -958.22 | 905.72 | -1,354.17** | -1,907.45*** |
| (0.024) | (1,175.4) | (2,096.8) | (569.8) | (423.8) |
| -0.110*** | 597.30 | 1,264.024 | 1,102.69** | 137.25 |

Results

Table 3 Multivariate results: household unsecured debt of single mothers, ages 19–55, 1988–1999 (2005\$)

| Variable | All single women (1) | Quant reg 75th percentile (2) | IHS (3) |
|---------------------------|-------------------------|----------------------------------|----------------------|
| 2 or more children (1995) | 180.74 (602.5) | −909.23*** (314.1) | −0.889*** (0.225) |
| 2 or more children *1988 | −1,488.69* (810.19) | 174.12 (521.0) | 0.080 (0.378) |
| 2 or more children *1991 | −1,571.84 (1,715.5) | 150.69 (416.7) | 0.380 (0.261) |
| 2 or more children *1993 | −1,203.99 (1,282.32) | 528.01 (392.8) | 0.218 (0.274) |
| 2 or more children *1996 | −1,648.99** (671.5) | −986.40*** (373.9) | −0.108 (0.293) |
| 2 or more children *1997 | −1,801.56** (764.5) | −818.77** (382.7) | 0.134 (0.286) |
| 2 or more children *1999 | −1,171.20 (846.571) | −1,468.32*** (397.0) | −0.113 (0.325) |

Discussion

- The past few decades have been a period of substantial growth in unsecured debt
- Also a period of growth in the EITC
- Between 1988-1999, single mothers bucked the national trend of rising unsecured debt
- It looks like they used part of their EITC to do this
- If so, the EITC may be making an important contribution to the financial stability of these households
- The EITC represents, perhaps, an underappreciated, but radical transformation of our safety net