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Growth and Decline in Tax Credits For Families With Children

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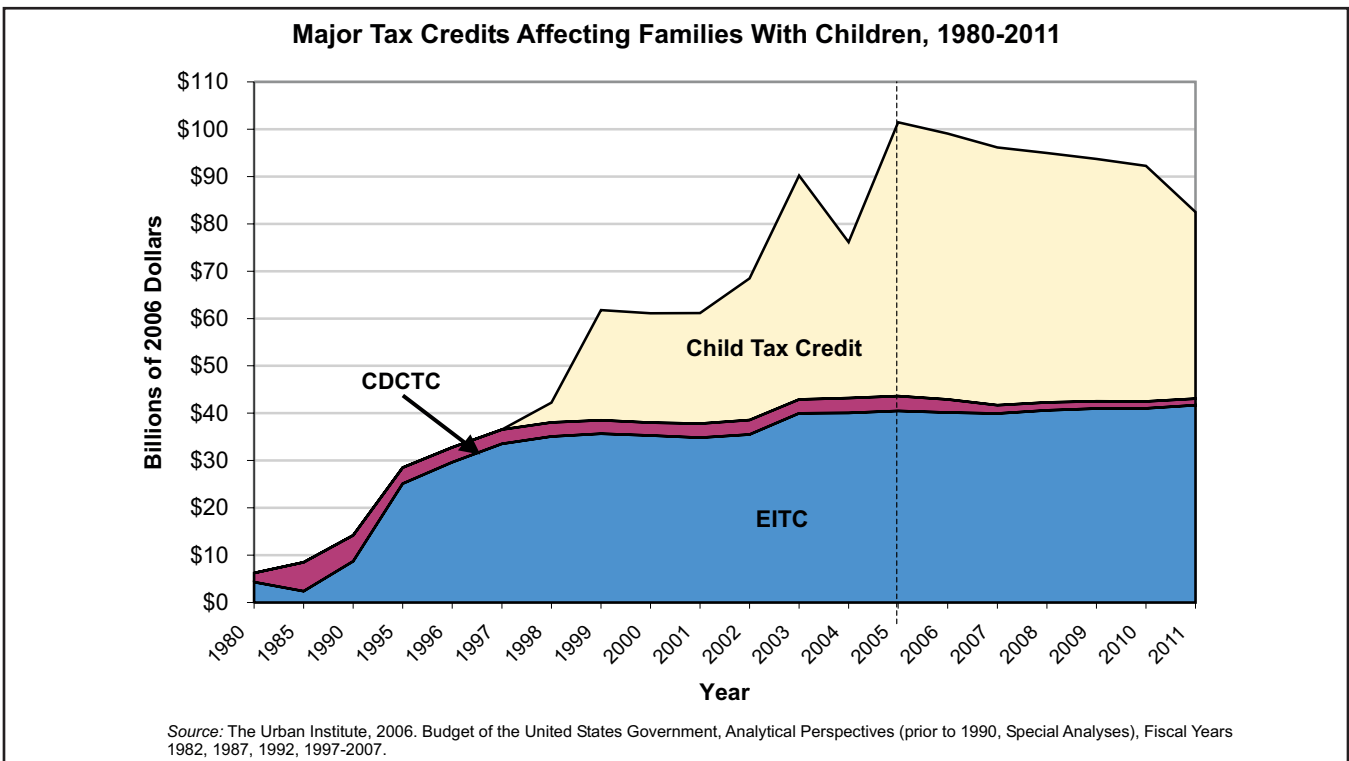
Under current law, there are three major tax credits that affect families with children: the earned income tax credit, the child and dependent care tax credit (CDCTC), and the child tax credit (CTC).

The EITC was enacted in 1975 to provide a credit to low-income working taxpayers with qualifying children (beginning in tax year 1994, taxpayers without a qualifying child became eligible to claim a small EITC). The CDCTC, also enacted in 1975, replaced the dependent care tax deduction, allowing taxpayers to claim a nonrefundable credit against their income tax.

As seen in the chart below, the revenue loss from the CDCTC has slowly declined since 1980, partly because it was not indexed for inflation. In contrast, expenditures on the EITC have grown because of expansions passed in

1986, 1990, 1993, and 2001, have been indexed for inflation since 1986, and are expected to plateau at around \$40 billion through 2011. Since the EITC is fully refundable, much of this growth comes from outlays to taxpayers rather than revenue loss.

Taken together, the EITC and the CDCTC were the major tax expenditures (except for the dependent exemption) on children through the late 1990s. In 1997, however, the Taxpayer Relief Act enacted the CTC, a \$500 tax credit for each qualifying child under the age of 17. This credit was increased to \$1,000 beginning in 2003. The child credit was refundable to the extent of 10 percent of the taxpayer's earned income in excess of \$10,500 (indexed for inflation) in 2003 and 15 percent for calendar year 2005 and thereafter. Since the \$1,000 maximum is not indexed for inflation, however, the real cost of the credit declines in value after peaking at \$58 billion in 2005. Its maximum amount of \$1,000 reverts to \$500 after 2010 unless the increase is further extended or made permanent.



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