

## Boosting incomes for Iowa families

### American Rescue Plan tax credits benefit 9 in 10 Iowa children

By now, many of us have seen the first of many benefits of the American Rescue Plan (ARP) — funds deposited in our bank accounts. The COVID-19 recovery bill passed by Congress and signed by President Biden March 12 authorized the payment of \$1,400 per person for every adult and child in a household with income below the threshold: \$75,000 for single adults, or \$150,000 for a couple.

Much more is to come: assistance in paying rent and utilities; help covering the cost of food, health insurance, and child care; the extension of much needed unemployment benefits. Altogether, the ARP will provide about \$960 billion in direct assistance to Americans, representing over half of the total cost of the legislation. We focus here on a less well-known portion of that assistance: \$100 billion in tax credits for individuals. Together these credit expansions will put as much as \$12,000 or \$14,000 in additional funds in the pockets of an Iowa family, and will benefit an estimated 93 percent of Iowa's children as well as 181,000 low-wage workers without children.<sup>1</sup>

All this help comes at a time when millions of Americans are still reeling from the effects of the yearlong battle with COVID-19 and the recession triggered by the extraordinary measures needed to contain the pandemic. While the economic recovery began last summer, it has stalled in recent months. There are still 80,400 fewer jobs in Iowa than just before the pandemic (February of 2020); nearly a third of those lost jobs are in the leisure and hospitality sector.<sup>2</sup> Job growth since November has been essentially zero.

In Iowa as in the country as a whole, the unemployment rate conceals a harsh reality: Thousands of Iowans have dropped out of the labor force in the past year and are no longer counted among the unemployed. The Iowa labor force has shrunk by nearly 100,000 since February of 2020.<sup>3</sup> For some, jobs simply disappeared, while others were forced to stay at home to care for children and to supervise their education. Those unemployed or forced out of the labor market are disproportionately women and persons of color. Women represented 41 percent of the unemployed in Iowa in 2019, 47 percent in 2020.<sup>4</sup>

The ARP provides assistance to the millions suffering the effects of the pandemic recession and at the same time pumps billions of dollars into the economy to get the recovery back on track. The recovery rebate checks and the extended unemployment benefits add up to \$600 billion that will very quickly boost consumer spending, which in turn helps businesses get back on their feet.

#### ► Credits provide a large boost to incomes in 2021

Two credits for families with children are raised dramatically for 2021 by the ARP. One is the Child Tax Credit (CTC), which is available to all families with children under age 17 living at home. The other is the Child and Dependent Care Credit (CDCC), which covers a portion of the cost of care for children and other dependents. The ARP increases the amount of the CTC, more than doubles the limit on the amount of child care expenses that are subject to the CDCC, dramatically raises the percentage of child care expenses allowed as a credit,

and makes both credits fully refundable: If the credit exceeds the amount of federal income tax due, the excess credit is paid as a refund. Iowa does not have a version of the federal CTC, but it does have a state CDCC, which is simply a percentage of the federal CDCC, and which already is refundable. The increase in the federal CDCC will automatically result in a larger state CDCC when families file their income taxes next year.

These changes will significantly boost the incomes of thousands of Iowa families. Importantly, families will not need to wait until they file their taxes next year to receive the CTC. The plan is to start making periodic payments in July of up to \$300 per child to families who qualify under the new rules based on their 2019 or 2020 income tax return; the remaining credit (roughly half) will be received when they file their 2021 tax return. The Child Tax Credit increase alone will benefit an estimated 669,000 Iowa children — 93 percent of the children under age 18 in the state — and will lift an estimated 25,000 Iowa children above the poverty line.<sup>5</sup>

In the table below we show the combined effects of the ARP changes in the CDC and the CDCC on federal and state income taxes for seven Iowa families, with children of different ages and different child care needs. The table shows the dollar benefits from ARP, in the form of reduced taxes and/or increased tax refunds. The illustrations are for families where all adults work full time and earn \$10 per hour. Child care costs were assumed to be at the statewide average for a licensed home, including before and after school care for children age 6-11.

**Table 1. ARP tax credit expansions will boost family incomes by thousands**

Net change in federal and state taxes due to ARP

Typical families in Iowa with parents earning \$10 per hour

	Benefit from Tax Credit		
	Federal	State	Total
<b>Married Couple</b>			
With one child under 6	\$4,361	\$1,104	\$5,465
With one child under 6, one age 6-11	\$7,556	\$1,658	\$9,214
With two children over age 6	\$9,473	\$2,185	\$11,658
With three children over age 6	\$5,224	\$578	\$5,802
<b>Single Parent</b>			
With one child under 6	\$5,391	\$1,580	\$6,971
With two children age 6-11	\$7,204	\$1,449	\$8,653
With two children under age 6	\$10,978	\$3,122	\$14,100

► **Earned Income Tax Credit helps childless workers**

The third major tax credit change involves the Earned Income Tax Credit (EITC). The Federal EITC provides substantial help to lower wage workers raising children. But single or married childless workers received a much smaller credit. In fact, many such workers were effectively taxed into poverty because of the low EITC. Under the ARP, this lower “childless EITC” is nearly tripled to reflect the devastating effects of the recession on low wage workers, whether raising a family or not. The maximum credit is raised from \$543 to \$1,502 and the income ceiling for receiving some benefit is raised from \$15,980 to \$21,430.

The Iowa EITC is simply 15 percent of the federal. As a result of ARP, low-wage childless individuals and couples will thus automatically receive a higher state EITC. A single person working full time at minimum wage would receive an additional \$902 in federal EITC and then another \$125 from the state credit as a result of ARP.

## ► **How the Child Tax Credit increase works**

The largest of the ARP tax credit changes is the child tax credit (CTC), available to families with children living at home and under age 17. Currently, 198,000 children in Iowa do not receive the full \$2,000 CTC because their families lack earnings or have earnings that are too low to get the maximum credit.<sup>6</sup> The current CTC increases with a family's earnings, up to the maximum credit, and is partially refundable – the so-called “additional child tax credit” available to low income families is refunded to the taxpayer if the credit exceeds the amount of income tax otherwise due. The ARP makes the entire credit available to all poor and middle class families for 2021, and raises the maximum credit from \$2,000 per child under age 17 to \$3,600 per child under 6 and \$3,000 per child age 6 to 17. Married couples will receive the full amount of the extra credit if their family income is below \$150,000; at that point it begins to phase out. A single parent (filing as a head of household) will receive the full extra child tax credit until income reaches \$112,500.

## ► **The Child and Dependent Care Credit reduces childcare costs dramatically**

The federal Child and Dependent Care Credit (CDCC) covers a portion of the cost of care for children and other dependents, through a tax credit that is not refundable (it can reduce your taxes to zero but cannot produce a refund). The maximum amount of childcare expenses per year that can be covered under the existing credit is \$3,000 per child, or \$6,000 for two or more children. The ARP raises that maximum to \$8,000 (\$16,000 for two or more children) and makes the credit fully refundable. It also increases the maximum credit from 35 percent of childcare expenses for those with income under \$15,000, to 50 percent of expenses for those with income under \$125,000. These percentages decrease as income increases. The existing credit equals 20 percent of expenses for those with income above \$43,000. Under the ARP, the percentage is 20 percent for those with income between \$183,000 and \$400,000 and then declines until it reaches zero at income of \$438,000. As with the CTC, both changes are for calendar 2021 only.

The Iowa CDCC is equal to 75 percent of the federal for those with income below \$10,000, declining to 30 percent for those with income between \$40,000 and \$90,000 and then zero beyond that. (We assume that the Iowa Senate will pass and the Governor will sign HF230, which increases the income limit for the CDCC from \$45,000 to \$90,000, retroactive to Jan. 1, 2021). For lower income Iowans the dramatic increase in the federal CDCC means a substantial increase in the Iowa CDCC as well. A single parent, for example, with two children under 6 requiring full time care could face childcare costs of \$13,500 per year in a licensed home (more if in a childcare center, or if one was an infant). If she made \$18,000 per year, the federal CDCC for that family would be \$6,723, while the Iowa credit would be 65 percent of that, or another \$4,370. The combined credit of \$11,092 would cover 82 percent of child care costs.

Changes in the income of families with children have been greatly expanded under the new federal COVID-19 assistance. For now it is limited but it may become so popular that some changes may become permanent.

## Appendix Table

Net savings in federal and state taxes due to ARP  
2021 tax law pre-ARP vs. 2021 tax law with ARP

Family type and hourly wage*	Increase in Federal Credits		Net Reduction in		Total tax
	Child Tax Credit	Child and Dependent Care Credit	Federal income tax	State income tax**	
<b>Single, childless</b>					
\$7.25	\$-	\$-	\$902	\$135	\$1,038
\$9.00	-	-	414	62	476
<b>Married, 1 child under 6</b>					
\$7.25	2,200	2,885	5,085	1,290	6,375
\$10	1,600	2,761	4,361	1,104	5,465
\$12	1,600	2,791	4,391	837*	5,228
<b>Married, 1 child under 6, 1 age 6-11</b>					
\$7.25	3,800	4,900	8,700	1,893	10,593
\$10	3,410	4,146	7,556	1,658	9,214
\$12	2,600	4,206	6,806	1,262*	8,068
<b>Married, 1 child age 6-11, 2 children age 12-17</b>					
\$7.25	4,851	1,568	6,419	632	7,051
\$10	3,780	1,444	5,224	578	5,802
\$12	3,000	1,474	4,474	442*	4,916
<b>Married, 2 children under 6</b>					
\$7.25	4,400	6,217	10,617	2,551	13,168
\$10	4,010	5,463	9,473	2,185	11,658
\$12	3,200	5,523	8,723	1,657*	10,380
<b>Single parent 1 child under 6</b>					
\$7.25	2,200	3,391	5,591	1,541	7,132
\$10	2,200	3,191	5,391	1,580	6,971
\$12	2,200	2,775	4,975	1,370	6,345
\$20	1,600	2,761	4,361	1,104	5,465
<b>Single parent, 2 children age 6-11</b>					
\$7.25	4,113	4,149	8,262	1,371	9,633
\$10	3,255	3,949	7,204	1,449	8,653
\$12	3,200	3,533	6,733	1,292	8,025
\$20	2,008	2,889	4,897	1,156	6,053
<b>Single parent, 2 children under 6</b>					
\$7.25	5,313	6,723	12,036	3,044	15,080
\$10	4,455	6,523	10,978	3,122	14,100
\$12	4,400	6,107	10,507	2,707	13,214
\$20	3,208	5,463	8,671	2,185	10,856

NOTE: All adults assumed to work full time year round

\*These amounts assume that legislation is passed this session raising the income ceiling on Iowa's Child and Dependent Care Credit from \$45,000 to \$90,000. Under existing law, these amounts would be zero.

\*\*For single person, this represents the Iowa EITC. For families with children, this amount represents the Iowa Child and Dependent Care Credit.

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<sup>1</sup> Center on Budget and Policy Priorities. American Rescue Plan Act Will Help Millions and Bolster the Economy. March 10, 2021.

<sup>2</sup> Iowa Workforce Development, Press Release, March 26, 2021. <https://www.iowaworkforcedevelopment.gov/iowas-unemployment-rate-36-percent-february>

<sup>3</sup> Iowa Workforce Development, Press Release, March 26, 2021.

<sup>4</sup> U.S. Bureau of Labor Statistics, Expanded State Employment Status Demographic Data. <https://www.bls.gov/lau/ex14tables.htm>

<sup>5</sup> Center on Budget and Policy Priorities. American Rescue Plan Act Will Help Millions and Bolster the Economy. March 10, 2021.

<sup>6</sup> Center on Budget and Policy Priorities. American Rescue Plan Act Will Help Millions and Bolster the Economy. March 10, 2021.