



Keeping What They've Earned: Tax Credits for Working Families in South Carolina

For millions of hard-working Americans, tax season means a trip to a commercial tax preparer to have their returns completed. For low- to moderate-income workers who may be eligible for the Earned Income Tax Credit (EITC), a credit designed to help working families continue working, the costs of tax preparation and other fees will decrease the amount of their tax refund. Fortunately, there are other options. The Volunteer Income Tax Assistance (VITA) program offers free electronic tax filing and direct deposit of refunds so that taxpayers can get their refunds in about 10 days without paying exorbitant fees. With the money saved, families can work towards financial stability by paying bills, making down payments on houses, and increasing savings.

Though millions of families will claim billions of dollars in EITC refunds this tax season, a large percentage of these taxpayers will pay outrageous fees to have their taxes prepared and to receive their refund more quickly. According to data from the Internal Revenue Service (IRS), recent success in promoting the EITC has been accompanied by losses to commercial tax preparers and Refund Anticipation Loan (RAL) lenders:

- More than 21.7 million taxpayers received the EITC in 2004, representing a \$39.8 billion investment in children, families, and the communities in which they live, work, and play. Tax preparation fees and RALs drained nearly \$2.9 billion from this investment.¹
- In South Carolina, over 422,000 taxpayers claimed an estimated \$814.6 million in Earned Income Tax Credits. These EITC claims composed almost two percent of the national total, but South Carolinians lost an estimated \$67 million to tax preparation fees and high interest loans.

Supports for Working Families

Each year, the EITC lifts nearly 5 million Americans above the poverty line.² Its contribution to the well-being of lower-wage, working families is significant—giving working parents an opportunity to support their families and infusing money into the local economy.³ For tax year 2006, this federal tax credit is worth up to:

- \$4,536 for families with two or more children;
- \$2,747 for families with one child; and,
- \$412 for individuals between the ages of 25 and 64 with no children.

In addition, many EITC recipients are also eligible for other tax credits such as the Child Tax Credit (CTC). The CTC is a federal tax credit for working families with children and incomes above \$11,300 and it is worth up to \$1,000 for each child claimed in tax year 2006. In 2004, the average total refund for South Carolina taxpayers claiming the EITC who also received other tax credits was \$3,041.

Costs of Using Commercial Tax Preparers and Refund Anticipation Loans

In order to claim the EITC and CTC, taxpayers must file their federal and state tax returns. This task can be quite challenging, as large numbers of EITC-eligible families hire commercial preparers to complete their returns. In 2004, almost 78 percent of EITC recipients in South Carolina paid to have their return completed professionally. Tax preparation fees drained over \$49 million from the pockets of working families.

In addition to paying high fees to commercial tax preparers, many working families also use Refund Anticipation Loans to get their refund money on the same day or within a few days. These short-term, high-interest loans are based on the filer's expected tax refund and can end up costing a taxpayer a large percentage of their refund. In 2004, the average family in South Carolina purchasing a RAL paid \$100 just to get their refund one or two weeks sooner—meaning that hard-working families lost \$18 million in RAL fees. What's more troubling is that EITC recipients are about six times as likely to purchase a RAL than taxpayers who did not file for the credit. According to IRS data, almost 180,000—or 44 percent—of South Carolina's EITC tax filers receiving refunds for 2004 also took out RALs, whereas approximately seven percent of non-EITC taxpayers who received refunds purchased RALs for the same year. Figure 1 illustrates the disproportionate usage of RALs by EITC families in the state's largest cities. Between the costs of tax preparation and RAL fees, the typical EITC family in South Carolina family

Figure 1: EITC v. Non-EITC Filers who Purchased Refund Anticipation Loans (RALs)

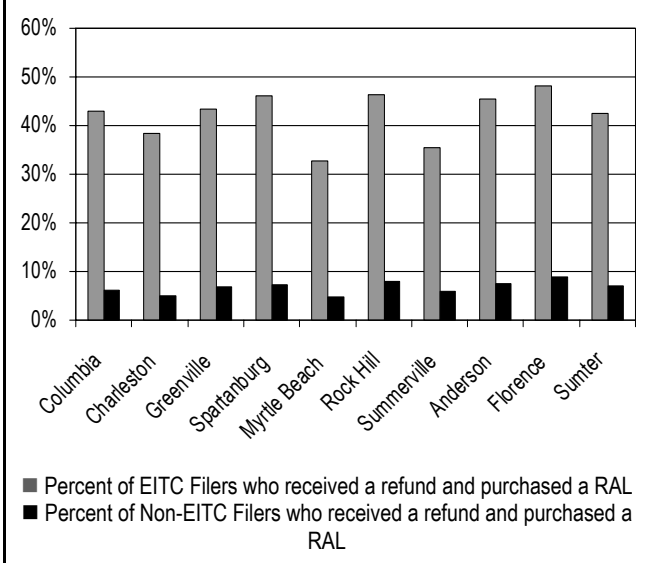


Figure 2: Total Dollars Lost to Tax Preparation and the Purchase of RALs in Cities with the Highest Total Number of Returns Filed, Tax Year 2004

City	Total Returns	EITC Returns	% of EITC Filers who used Paid Preparers	% of EITC Returns with a RAL*	% of Non-EITC Returns with a RAL*	Dollars Lost to Tax Prep and RALs**	Child Poverty Rate
Columbia	130,416	28,525	72.1%	43.0%	6.1%	\$4,285,860.00	30.2%
Charleston	79,824	15,008	75.8%	38.3%	4.9%	\$2,262,900.00	24.8%
Greenville	78,785	17,204	78.9%	43.5%	6.8%	\$2,763,060.00	23.1%
Spartanburg	49,554	11,547	80.2%	46.1%	7.3%	\$1,908,150.00	34.7%
Myrtle Beach	47,659	8,225	71.0%	32.8%	4.7%	\$1,133,040.00	17.8%
Rock Hill	41,226	8,831	78.6%	46.3%	8.0%	\$1,441,170.00	16.7%
Summerville	40,252	7,288	73.2%	35.4%	5.9%	\$1,051,260.00	10.3%
Anderson	36,476	8,198	79.1%	45.5%	7.4%	\$1,335,960.00	30.6%
Florence	35,606	9,028	79.3%	48.1%	8.8%	\$1,499,880.00	28.5%
Sumter	33,718	10,230	76.9%	42.5%	7.0%	\$1,605,480.00	22.0%
SC Totals	1,797,085	422,511	77.6%	43.7%	7.2%	\$67,156,260	18.8%
US Totals	128,599,631	21,721,218	70.6%	28.8%	4.5%	\$2,896,229,700	16.6%

Source: Internal Revenue Service SPEC Information Database, Tax Year 2004 (December 2006). Poverty figures from US Census Bureau 2000 Census. CDF calculations.

*Of those who received a refund

**Calculated based on a \$150 average tax preparation fee and a \$100 average RAL fee.

getting a RAL loses an estimated 5.4 percent of its federal refund.

Although RAL usage dropped significantly in 2004, new industry developments put lower-wage families at greater financial risk.⁴ Vendors introduced the pay stub or holiday RAL, which is available to taxpayers prior to receiving their W-2s and is taken out against their expected return. As advocates educate taxpayers about the dangers of purchasing RALs, lenders are finding more ways to reach taxpayers earlier. These developments hurt community efforts to encourage the use of free tax filing sites because loans are now accessible before the tax season begins. To complicate matters, some preparation businesses were requiring pay stub and holiday RAL users to return to the same office once more to have their tax returns completed.⁵

Effects on Economic Activity

RAL fees and tax preparation costs represent a significant drain on local economies across South Carolina. Figure 2 summarizes the total dollars lost in South Carolina's largest cities, while Figures 3 and 4 highlight the losses endured at the county level. Figure 4, in particular, highlights the troubles faced by families in the Pee Dee region of the state. Four of the top six counties in the state with the highest percentage of RAL purchases are located in this region. More troubling, Dillon, Marlboro, and Bamberg counties have some of the highest RAL purchase rates among EITC claimants in the country.

Additionally, these figures reveal that counties with high rates of RAL usage also tend to have higher rates of child poverty. The average child poverty rate in South Carolina's 10 counties with the highest percentage of RALs was 27.2 percent, higher than the state-wide rate of 18.8 and the national rate of 16.6 percent.

While only a handful of studies have measured the economic impact of the Earned Income Tax Credit on local economies, their results are telling. An analysis of EITC population and participation rates by researchers in San Antonio concluded that increasing the number of EITC claims would benefit the city's economy. Not only would two-thirds of additional EITC dollars be spent locally on retail, general services and utilities, but each additional dollar received would generate roughly \$1.58 in local economic activity.⁶ Unfortunately, cities such as San Antonio do not benefit fully from increasing EITC participation rates because money that was intended for working families is diverted into the portfolios of commercial tax preparers and lending institutions. South Carolina communities are similarly affected because fewer dollars in the hands of working families means less economic activity.

Recommendations

South Carolina families lost an estimated \$67 million because of tax preparation fees and RALs in 2004. Government officials and community leaders are in a unique position to develop public policies that address the cause and mitigate the effect of RALs and costly tax preparation on lower-income communities. To that end, Children's Defense Fund recommends the following:

1. **Strengthen consumer protections.** South Carolina lawmakers must consider adopting policies that establish licensing requirements for commercial tax preparers, ensure full disclosure of RAL fees and interest rates, prohibit the sale of RALs to EITC recipients, and place a cap on the interest rates that banks can charge for RALs.
2. **Expand access to free tax assistance.** Large numbers of South Carolinians pay to have their taxes completed and filed. Elected officials and community

Figure 3: Total Dollars Lost to Tax Preparation and RALs in South Carolina Counties with the Highest Number of Total Returns Filed, Tax Year 2004

County	Total Returns	EITC Returns	% of EITC Filers who used Paid Preparers	% of EITC Returns with a RAL*	% of Non-EITC Returns with a RAL*	Dollars Lost to Tax Prep and RALs**	Child Poverty Rate
Greenville	182,677	33,440	76.9%	39.2%	5.9%	\$5,124,120	13.7%
Charleston	151,247	29,917	77.0%	39.5%	5.0%	\$4,603,350	23.3%
Richland	146,432	32,396	72.0%	42.5%	6.2%	\$4,848,240	17.9%
Horry	110,742	22,894	73.0%	37.1%	5.1%	\$3,321,390	18.3%
Spartanburg	108,831	24,166	80.3%	43.2%	7.7%	\$3,923,820	15.5%
Lexington	105,141	17,690	72.8%	35.7%	5.1%	\$2,539,860	11.4%
York	84,539	15,981	78.8%	44.3%	7.7%	\$2,575,740	12.3%
Anderson	66,912	15,063	79.7%	43.4%	8.1%	\$2,435,790	15.7%
Aiken	63,045	13,994	76.9%	37.6%	5.6%	\$2,123,430	19.3%
Beaufort	61,502	10,282	69.9%	39.1%	5.5%	\$1,467,090	15.7%
Florence	57,786	16,994	80.8%	49.2%	10.1%	\$2,876,460	22.7%
Dorchester	55,871	11,463	74.8%	39.3%	6.5%	\$1,724,040	11.9%
Berkeley	54,512	12,049	77.7%	37.4%	7.1%	\$1,843,770	15.9%
Pickens	48,995	8,864	79.0%	36.4%	6.2%	\$1,359,240	12.6%
Sumter	44,507	13,906	75.6%	42.4%	7.6%	\$2,154,960	21.7%
Orangeburg	37,942	13,392	78.2%	52.1%	10.7%	\$2,255,790	27.6%
Oconee	29,692	5,496	81.2%	36.3%	5.9%	\$860,670	14.6%
Greenwood	28,680	7,444	80.3%	45.7%	7.7%	\$1,228,710	18.2%
Darlington	26,973	8,949	81.9%	50.8%	12.3%	\$1,545,330	27.0%
Kershaw	25,756	5,673	78.8%	39.7%	7.0%	\$889,620	17.2%
Lancaster	23,908	6,375	89.0%	49.2%	10.9%	\$1,157,430	16.9%
Georgetown	22,339	6,279	79.1%	40.7%	6.5%	\$994,740	26.0%
Laurens	22,040	6,541	84.9%	52.2%	10.0%	\$1,165,860	20.1%
Cherokee	19,344	5,463	80.9%	48.9%	9.3%	\$926,130	17.0%
Chesterfield	16,690	5,609	89.5%	54.0%	15.4%	\$1,049,430	25.0%
SC Totals	1,797,085	422,511	77.6%	43.7%	7.2%	\$67,156,260	18.8%
US Totals	128,599,631	21,721,218	70.6%	28.8%	4.5%	\$2,896,229,700	16.6%

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- leaders must find ways to build and maintain free tax preparation networks throughout the state by investing in the Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) programs and other free tax assistance centers.
3. *Connect working families to mainstream financial services.* Free or low-cost checking and savings accounts, credit counseling opportunities, and financial education programs offer working families the tools to build for a better financial future, and public – private partnerships should be explored and established to ensure that working families have easy access to these resources.

4. *Create a state EITC.* South Carolina does not have a state Earned Income Tax Credit. Most poor children live in families with a working parent and research indicates that tax refunds, including a state EITC refund, can be used to help families build assets while stimulating local economies. In December 2006, House Bill 3167 was introduced by Representatives Cobb-Hunter, Sellers, and Williams and later referred to the Committee on Ways and means. This bill would institute a state EITC equal to ten percent of the federal EITC with annual incremental increases up to twenty percent of the federal EITC.

Figure 4: South Carolina Counties with the Highest Percentage of Refund Anticipation Loan Purchases, Tax Year 2004

County	Total Returns	EITC Returns	% of EITC Filers who used Paid Preparers	% of EITC Returns with a RAL*	% of Non-EITC Returns with a RAL*	Dollars Lost to Tax Prep and RALs**	Child Poverty Rate
Dillon	12,256	5,279	76.2%	60.1%	15.6%	\$915,450	33.4%
Marlboro	11,319	4,937	80.6%	57.9%	14.8%	\$879,690	29.4%
Bamberg	5,771	2,303	67.6%	56.5%	13.9%	\$360,090	35.4%
Jasper	7,346	2,652	82.7%	54.4%	14.2%	\$469,470	26.5%
Chesterfield	16,690	5,609	89.5%	54.0%	15.4%	\$1,049,430	25.0%
Marion	13,389	5,691	75.5%	52.8%	11.7%	\$940,950	33.6%
Chester	14,295	4,387	77.7%	52.7%	12.8%	\$738,330	21.5%
Edgefield	6,688	2,124	79.9%	52.2%	12.1%	\$363,000	19.8%
Laurens	22,040	6,541	84.9%	52.2%	10.0%	\$1,165,860	20.1%
Orangeburg	37,942	13,392	78.2%	52.1%	10.7%	\$2,255,790	27.6%
Lee	6,441	2,819	77.2%	52.1%	11.8%	\$470,790	25.8%
Allendale	3,704	1,795	83.8%	51.9%	12.4%	\$317,850	48.1%
Calhoun	4,523	1,401	73.9%	51.7%	10.8%	\$226,350	20.5%
Union	11,652	3,375	84.1%	51.0%	11.0%	\$594,060	19.4%
Darlington	26,973	8,949	81.9%	50.8%	12.3%	\$1,545,330	27.0%
Clarendon	12,400	4,607	81.0%	50.6%	10.3%	\$787,890	28.2%
Abbeville	8,477	2,573	81.0%	50.3%	11.5%	\$439,080	17.8%
Barnwell	9,287	3,227	75.2%	49.7%	9.8%	\$521,160	27.7%
Williamsburg	12,966	5,837	78.4%	49.6%	11.7%	\$972,000	36.2%
Florence	57,786	16,994	80.8%	49.2%	10.1%	\$2,876,460	26.0%
McCormick	4,361	1,282	85.6%	49.2%	11.2%	\$226,470	26.6%
Lancaster	23,908	6,375	89.0%	49.2%	10.9%	\$1,157,430	16.9%
Cherokee	19,344	5,463	80.9%	48.9%	9.3%	\$926,130	17.0%
Newberry	16,051	4,103	77.0%	47.6%	7.3%	\$665,400	23.7%
Saluda	5,363	1,643	78.1%	47.2%	11.3%	\$267,480	21.9%
SC Totals	1,797,085	422,511	77.6%	43.7%	7.2%	\$67,156,260	18.8%
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ENDNOTES

1. IRS SPEC Return Information Database, Tax Year 2004 (December 2006). All figures contained in this report have been retrieved from the 2004 SPEC database unless otherwise noted. CDF calculations.
2. Alan Berube, *Using the Earned Income Tax Credit to Stimulate Local Economies* (The Living Cities Policy Series, 2007).
3. Steve Holt, *The Earned Income Tax Credit at Age 30: What We Know* (Washington: Brookings Institution, 2006).
4. The number and cost of RALs purchased declined significantly in the 2004 tax year, possibly due to more education and awareness, advocacy, and changes to IRS reporting. Chi Chi Wu, *One Step Forward, One Step Back: Progress Seen in Efforts Against High-Priced Refund Anticipation Loans, but Even More Abusive Products Introduced* (Boston: National Consumer Law Center, 2007).
5. Chi Chi Wu, *One Step Forward, One Step Back*.
6. *2004 Update: Increased Participation in the Earned Income Tax Credit in San Antonio* (Austin: Texas Perspectives, 2004). CDF calculations.

Children's Defense Fund®

Healthy Child Campaign



In addition to the EITC and access to VITA sites, health insurance is critical to financial stability. Health care costs have increased drastically in recent years, leaving an estimated 9 million children uninsured. Families that lack medical insurance tend to have higher credit card debt because they cannot pay for services, and, as a result, medical expenses account for nearly 50 percent of bankruptcy filings. CDF unveiled a legislative proposal in January that would ensure that all children would receive coverage for all medically necessary care. For more information, visit www.childrensdefense.org/healthychild.