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Claims That Stimulus Tax Cuts Go to "People Who Don't Pay Taxes" Are Intentionally Misleading

Some members of Congress lately are fond of saying that refundable tax credit (credits against tax that can result in the IRS actually sending money to taxpayers instead of taking money from them) amount to "tax cuts for people who don't pay taxes." This is intentionally misleading. Essentially all working families pay federal payroll taxes (and excise taxes like the federal gasoline tax and tobacco taxes), but many do not earn enough to owe any federal income tax. Congress and presidents since Jimmy Carter (including President George W. Bush) created or expanded refundable income tax credits, which can result in families of modest income having negative income tax liability.

The checks sent from the IRS to such taxpayers can be thought of as a way of offsetting payroll taxes for these families, because the main refundable credits are available only to people who work. This is true of the Earned Income Tax Credit (EITC). It's also true of the refundable portion of the Child Tax Credit (CTC) which is limited to a fraction of earnings or $1,000 per child, whichever is less. It's also true of the "Making Work Pay Credit" proposed by President Barack Obama and equal to 6.2 percent of earnings up to the maximum credit of $500 (or $1,000 for a couple). The stimulus bill passed by the House of Representatives this week would modestly expand the EITC and the refundable part of the CTC for low-income families, and would create, for two years, the Making Work Pay Credit.[1]

We project that 37.9% of taxpayers in the United States will not have positive income tax liability in 2009 under current law. Virtually everyone in this group who works pays federal payroll taxes, and even who those who don't work (because they are retired, etc.) pay federal excise taxes and a plethora of state sales taxes, property taxes and excise taxes.

Within this group there is a smaller group, 29.2% of all U.S. taxpayers in 2009, who do not even have enough income to be in the first income tax bracket. If a taxpayer's deductions (usually lower-income people just take the standard deduction) plus their exemptions add up to more than their income, then they do not have enough income to be in the first income tax bracket. This is true for a family of four in 2009 if their pre-tax income is below $26,000.[2]

These are people who would owe no federal income tax *even if there were no credits* (refundable or non-refundable). There is no possible way taxpayers in this group can benefit from a cut in the income tax unless it takes the form of a refundable credit. For example, the House GOP proposal to cut the bottom two rates could not help anyone in this group because their income is not subject to any federal income tax rate.

[1] For details and state-by-state estimates of the tax cuts included in the stimulus bill passed by the House, see Citizens for Tax Justice, "Less Than a Quarter of House GOP's Tax Rate Reduction Proposal Would Go to the Poorest 60% of Taxpayers," January 30, 2009. http://www.ctj.org/pdf/housestimulusupdate.pdf

[2] Couples with two children get four personal exemptions of $3,650 each, for a total of $14,600, plus a "standard deduction" of $11,400. Thus the first $26,000 in reported income is not taxed. Better-off taxpayers can substitute itemized deductions for the standard deduction if their itemized deductions are bigger.