

WHO TAKES CREDIT?:
THE EITC AND FREE TAX
PREPARATION IN CUYAHOGA
COUNTY, 2010

A REPORT FROM
POLICY MATTERS OHIO

DAVID ROTHSTEIN

JANUARY, 2011

AUTHOR

David Rothstein is a researcher at Policy Matters Ohio. He researches consumer protection, tax, asset building, and other economic policies. Rothstein sits on the Steering Committee for the National Community Tax Coalition and is the co-chair of the Policy and Advocacy Working Group. He has a master's in political science from Kent State University and a bachelor's degree from John Carroll University.

ACKNOWLEDGEMENTS

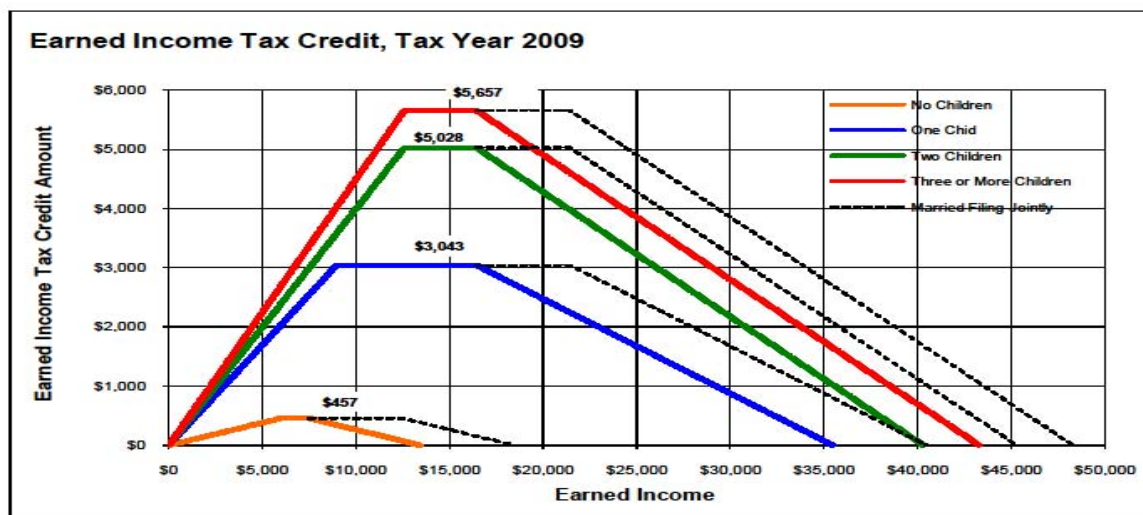
We thank the Cuyahoga EITC Coalition, the Cleveland Foundation, and the Pepsi Refresh Project for their generous support for this project. All errors and omissions are the sole responsibility of the author.

POLICY MATTERS OHIO, the publisher of this study, is a nonprofit, nonpartisan policy institute dedicated to researching an economy that works for Ohio. Policy Matters seeks to broaden debate about economic policy by doing research on issues that matter to working people and their families. With better information, we can achieve more just and efficient economic policy. Areas of inquiry for Policy Matters include work, wages, education, housing, energy, tax and budget policy, and economic development.

The Cuyahoga EITC Coalition is a group of social service agencies, community groups, and government entities that provides free tax preparation for low- and middle-income families. During last year's tax season, the Coalition prepared more than 8,000 tax returns and returned more than \$11 million back to Cuyahoga County residents. Slightly less than one-third of clients (30 percent) received the Earned Income Tax Credit (EITC), which is a refundable federal tax credit that varies based on marital status, children, and income level. The EITC, targeted at families with children, can provide more than \$5,600 to a family due to changes made by the American Recovery and Reinvestment Act (see Figure 1).¹ As Figure 1 illustrates, married couples are eligible for higher EITC claims as the income limits increase. The revised EITC schedule includes coverage of a third child and a larger earnings threshold for married couples to claim the credit.

The EITC, available only to low- and moderate-income families who work and pay taxes, is the nation's largest program to help low-income families pay for basic needs. The EITC is a refundable tax credit: if the credit exceeds the amount owed, the government sends a refund check in the amount of the difference. Under the Recovery Act, the maximum EITC for a family with three qualifying children and income between \$12,620 to \$24,000 is \$5,657. The average EITC in Ohio in the first year of the ARRA was \$2,210.

In 2009, the EITC provided more than 950,000 Ohio families with total refunds of \$2.1 billion.² The EITC is the largest anti-poverty tax program in the nation, lifting an estimated 5 million children above the federal poverty line. Thus, the service delivery, like that provided by the Coalition, for claiming this and other credits for working families is crucial.



¹ "How Will Changes to the EITC in the American Recovery and Reinvestment Act Affect Working Families?" *Center for Economic Progress* (March 13, 2009): http://www.tax-coalition.org/materials/2009/Economic_Stimulus_EITC%20Summary_03.12.09.pdf

² Internal Revenue Service, "EITC State Statistics at-a-Glance for Tax Year 2009." <http://www.eitc.irs.gov/central/eitcstats/> (updated 10/21/2010).

In Cuyahoga County, the EITC provides significant assistance to working families (see Table 1). More than 114,000 families claim the EITC, bringing some \$235 million to the county. The average EITC in Cuyahoga County was \$2,047, however, many eligible families do not get the credit or do not receive all that they might. In a broader context, a \$2,000 refund represents 10 percent of a family's income at \$20,000 a year. Families are often unaware of the EITC, claim it incorrectly, or pay to have their taxes filed diluting portions of their refund. The IRS and Government Accountability Office estimate that up to 25 percent of eligible EITC filers do not claim the credit.³ The Cuyahoga EITC Coalition provides free tax assistance to help families claim all of their EITC and e-file their return. With an e-filed return, a client with direct deposit will likely receive their return in seven to 10 days. Some clients that use the Cuyahoga EITC Coalition's report direct deposits of their refunds in five days.

The free tax assistance efforts by the Coalition and Ohio Benefit Bank made sizable impacts in the last few years. First, there was a 4 percent drop in the percentage of EITC returns prepared by paid preparers from 2007 to 2008 in Cuyahoga County. Second, there were 3,000 less EITC filers purchasing tax loans or tax checks. Both of these decreases are in contrast the increases to the number of EITC claims. The Coalition and Ohio Benefit Bank have grown in sites and territory covered for free tax preparation.

Table 1: The Federal EITC in Cuyahoga County, 2008⁴

Total Returns	EITC Returns	Percentage EITC Returns	Total EITC Amount	Average EITC Amount	Total EITC Returns Filed with Paid Preparers	Percentage of EITC Returns Prepared by Paid Preparers	Total EITC Filers Purchasing Loans or Refund Checks
695,053	114,990	17%	\$235.4 million	\$2,047	70,439	61%	54,768

Many EITC claimants and low-income working families use paid tax preparation, which can cost them anywhere from \$100 to \$300 per refund. In Cuyahoga County, 61 percent of EITC filers paid for tax preparation. Additional costs to families who use paid tax preparation are tax refund anticipation loans (RALs), which are brokered loans from a third party lender to the filer through the paid tax preparer. These are short-term, high-interest loans that provide quick payment of the anticipated refund to the client. Most RALs or loan checks expedite the return process by several days, often getting filers a portion of their refund in a few days, but come at an additional price of \$60 to \$130. Many filers use the loan to pay for the cost of their tax preparation.⁵ New trends in the RAL

³ John Wancheck, "The Earned Income Tax Credit: A Fact Sheet," Center on Budget and Policy Priorities : (2009) <http://www.cbpp.org/eitc-partnership/eitcfactsheet.htm>.

⁴ Tax Year 2008 is the most recent data available for county-level breakdowns. Data was analyzed through the Brookings Institution, Metropolitan Policy Program: <http://www.brookings.edu/metro/EITC/EITC-Data.aspx>.

⁵ Chi Chi Wu and Jean Ann Fox. "Beginning of the End?: Major Changes to Quick Tax Refund Loan Industry," *National Consumer Law Center* (January 19, 2010): http://www.consumerlaw.org/issues/refund_anticipation/content/2010-RAL-earlyPR.pdf.

market suggest that banks are making fewer loans and taking longer to get them to clients.⁶ JP Morgan Chase and HSBC, the two leaders in RAL banking, will not make loans in the upcoming tax year. More than 54,000 EITC filers (52 percent of all EITC filers) in Cuyahoga County purchased tax loans or checks from paid preparers. Tax loans extract an estimated \$1 million from EITC claimants in Cuyahoga County. Paid tax preparation costs EITC claimants at least \$10 million. With less tax loans being sold, community tax preparation will likely see more new clients this year, coming earlier in the tax season.

⁶ Maria Aspan. "Tightening Screws on Refund Anticipation Loans," *American Banker* (January 12, 2010): http://www.americanbanker.com/issues/175_7/tightening-screws-on-tax-loans-1005978-1.html.

Coalition overview

The Cuyahoga EITC Coalition, in a six-year time span, has produced impressive results (see Table 2). Sites that prepare taxes do so under the federal Volunteer Income Tax Assistance (VITA) program. IRS trained and tested volunteers prepare federal, state, and local taxes.⁷ The Coalition increased client returns by nearly 300 percent since 2005. In 2010, the Coalition served 8,121 clients, bringing more than \$11 million (\$3.4 million in EITC) back to Cuyahoga County. There was a slight increase in the number of clients served from 2009 to 2010. Several factors outside of the Coalition's control, including a winter-storm during the busiest part of tax season and late changes to the federal tax code, impacted the total clients served. Some thirty percent of clients claimed the EITC, accounting for \$3.4 million of those refunds. The average client's total refund was \$1,366 with the average return containing an EITC being \$1,383. The six-year growth rate in total returns topped 300 percent this year.

Total Returns	6 Year Growth in Total Returns	EITC Returns	6 Year Growth in EITC Returns	Percentage EITC Returns	Total EITC Amount	Total Refund Amount	6 Year Growth in Total Refund Amount
8,121	304%	2,457	209%	30%	\$3.4 million	\$11.1 million	296%

Average Return with an EITC	Average Return
\$1,383	\$1,366

The overall share of EITC returns prepared by the Coalition grew significantly over the last six years but remains a small percentage (three) of all Cuyahoga County EITC returns. Nationally, around one percent of all EITC returns are prepared by free tax coalitions. Some EITC filers use paid preparation early in January before free tax sites are ready to assist them. However, our previous studies using focus groups and surveys suggest that the main reason for not using free tax preparation is the lack of knowledge and awareness of these services by clients.⁸ As noted earlier in the report, if the RAL product is substantially changed, the advantage of paid tax preparation for low-income working families would be less.

The Coalition increased its influence by providing marketing, technical assistance, and e-filing capabilities to other coalitions around the state. Specifically, Lucas and Lorain County utilized the

⁷ For more on the IRS VITA program, visit the IRS free services website at: <http://www.irs.gov/individuals/article/0,,id=107626,00.html>.

⁸ See David Rothstein and Piet van Lier "Connecting Free Tax Preparation and Asset Building: Cuyahoga EITC Coalition Study," *Policy Matters Ohio* (January, 2009): http://www.policymattersohio.org/pdf/FreeTaxPrep2009_0120.pdf.

Coalition for e-filing and tax preparation. Table 3, below, displays the results from these two growing coalitions around Ohio. These two additional Coalitions served nearly 3,000 clients, helping families claim \$3.8 million. Additionally, coalitions around the state receive marketing and technology support, often difficult to measure. First Call for Help/211 provides a 24 hour, bilingual, referral service for interested clients to any tax site that fits their needs. This includes referrals and marketing for the Ohio Benefit Bank and AARP who also offer free tax preparation and other services. This work is difficult to standardize and measure but is an important role for the Coalition.

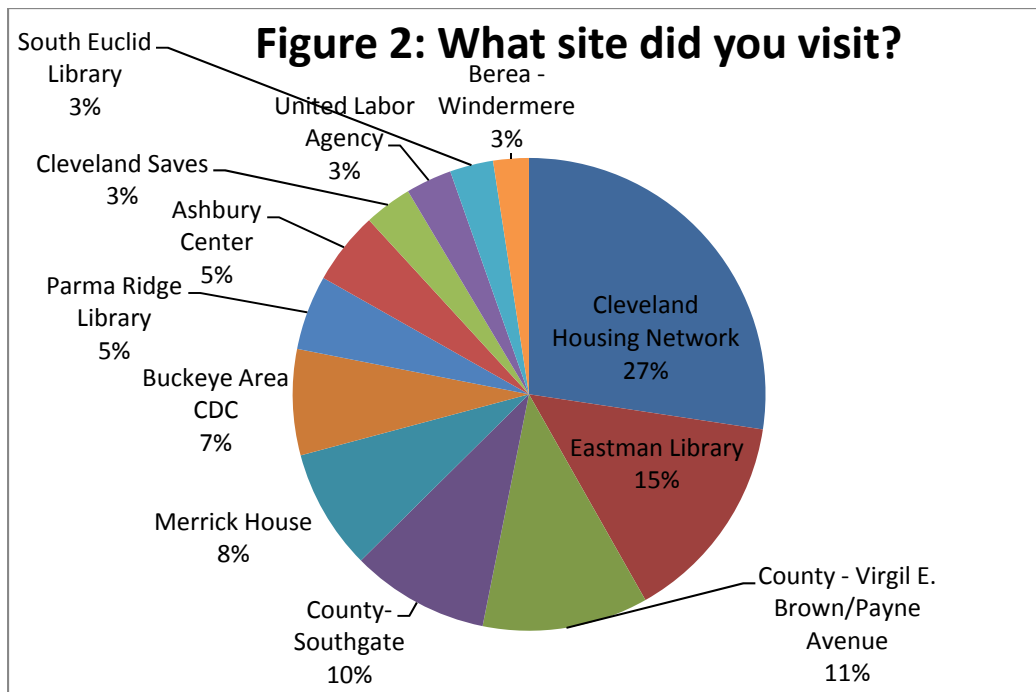
Table 3: 2010 Additional Coalition Results						
Coalition	Total Returns	EITC Returns	Percentage EITC Returns	Total EITC Amount	Average EITC Return	Total Refund Amount
Lorain	1,469	298	20%	\$600,000	\$2,013	\$1.7 million
Lucas	1,447	519	36%	\$ 719,574	\$1,386	\$2.1 million
Total	2,916	817	28%	\$1.3 million	\$1,615	\$3.8 million

Quantitative survey methodology

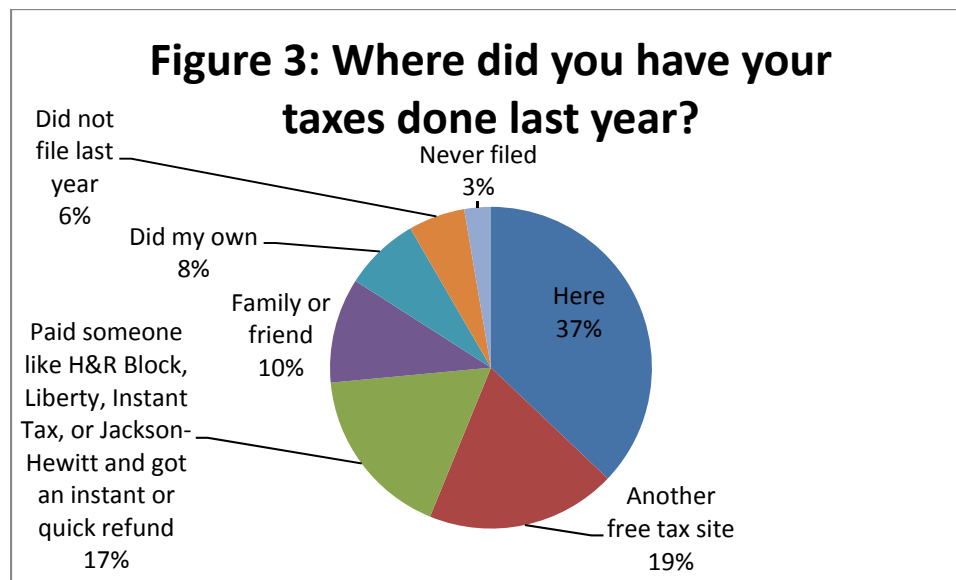
The Cuyahoga EITC Coalition commissioned Policy Matters Ohio to evaluate clients and the overall efforts of the Coalition. Twelve VITA sites distributed the survey and 1,600 clients participated. Clients were not required to fill out the survey to receive free tax preparation nor did they have to answer every question on the survey. More than 25 percent of all clients decided to participate in the survey. The goals of the survey were to understand what marketing efforts resonate with clients, how free tax services impact their lives, and how clients make financial choices. This year’s survey had a specific interest in understanding financial behavior of clients to understand the best ways to incorporate asset building into Coalition efforts. This survey also included more targeted questions and also asked about public assistance programs and barriers to saving. In past year surveys and focus groups, similar questions were asked but focused more on demographic characteristics and spending behavior of clients.

Survey Results

Twelve free tax sites participated in surveying clients (see Figure 3). Cleveland Housing Network, the Coalition’s largest site, surveyed the most clients with 461 responding. Taken together, two Cuyahoga County sites, Virgil E. Brown (191) and Southgate (159) with 350 surveys completed. The mixture of urban and suburban tax sites is important to understand the client base.

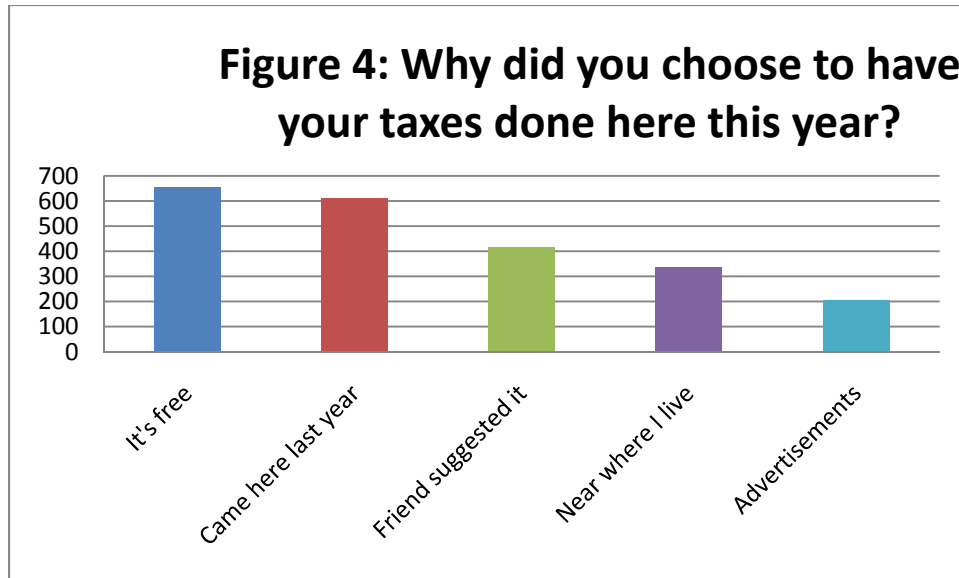


Of the 1685 survey participants, 44 percent had not used free tax services before this tax season. This is far less than the 60 percent who were first time clients in the previous year, indicating more return clients. Figure 3, below, displays how clients prepared their taxes the previous year. Seventeen percent of participants paid to have their taxes done, which is nearly half of the previous year's clients who paid for preparation. Far less clients did not file or used family and friends to help prepare taxes than in previous years. This survey marks the largest return clientele in five years of evaluation. Based on Coalition intake sheets, most sites continue to have repeat customers who file early in the tax season.

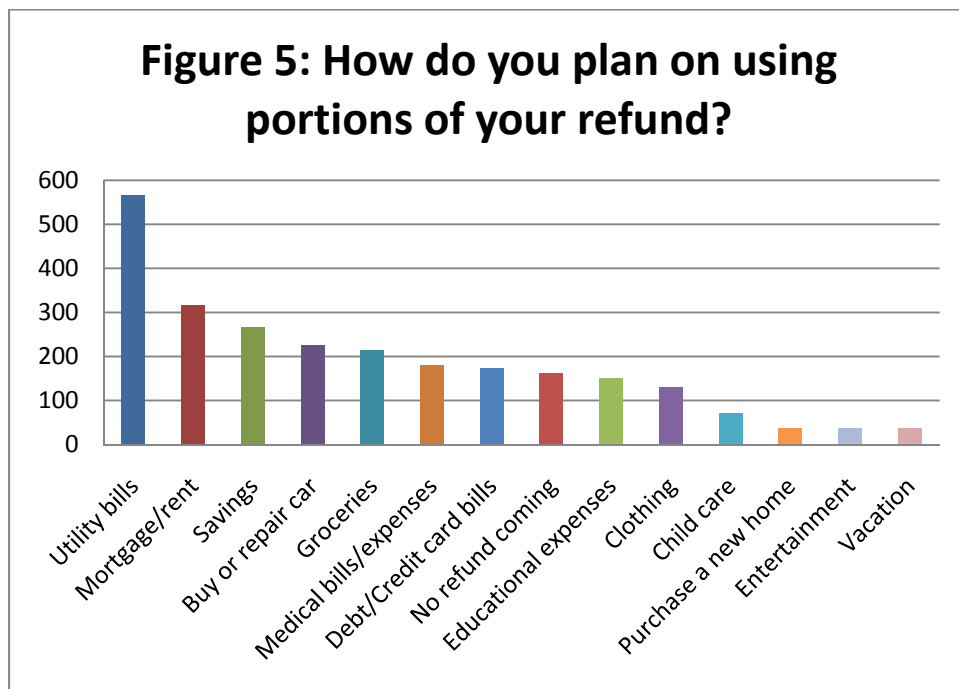


While clients heard about the Coalition from a variety of marketing efforts, word of mouth continues to be the way most clients hear about free tax preparation. More than 690 clients heard about the Coalition's services from friends and families, which is the most from any year surveyed. Clients continue to respond to social service agencies that offer free tax services and contact them directly through flyers or posters. Advertisements on the radio and in print also impacted how clients heard about the Coalition. Nationwide, radio has become a popular medium to reach working women. Most clients use the direct referral line of 2-1-1, First Call for Help, which is printed or mentioned on the majority of marketing material. In the current tax season, 2-1-1 will provide not only referrals but also make appointments for certain Super Saturday events and sites. The majority of clients reported at least three ways that they heard about the Coalition and its services, which exemplifies the Coalition's ability to get its message into multiple markets.

Clients expressed a variety of reasons for deciding to use free tax services from the Coalition (see Figure 4). The tax service being free continues to be the top reason for clients using the service but coming to the site the year before was a close second for the first time. While clients reported that a site being in their neighborhood was important, it once again was not among the top three reasons that clients used the Coalition.

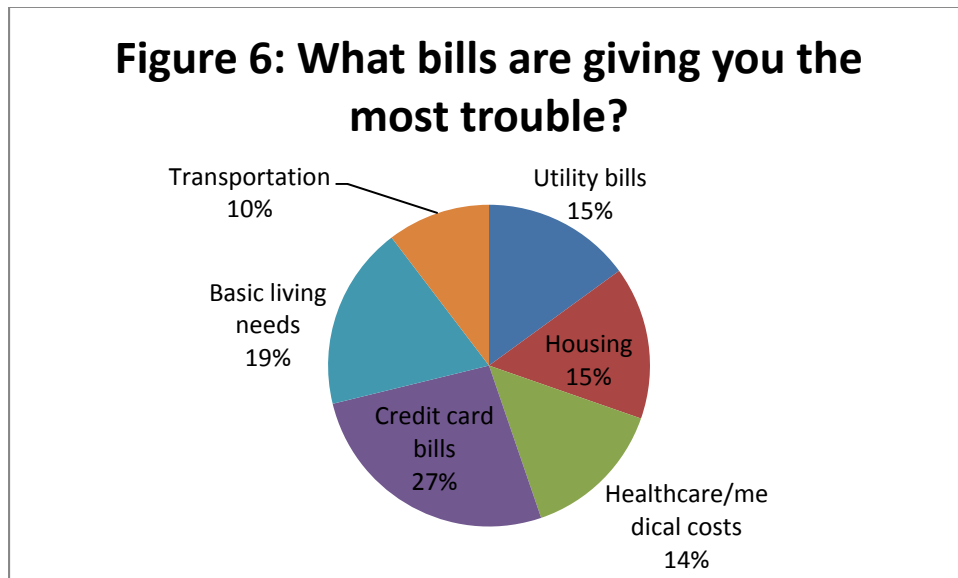


Clients indicated that they use their refunds for a variety of goods and services, often purchased in the local community. Data from the survey, displayed in Figure 5, indicates that refunds were used for basic living expenses such as utility bills, food and clothing, housing, and transportation expenses. Many who answered “other” indicated their refunds would be spent on their children, for child support, or back taxes. More than 260 clients indicated that they would save a portion of their refund, the third most popular response this year. Importantly, few clients indicated they would spend their refund on entertainment or vacation related purchases.

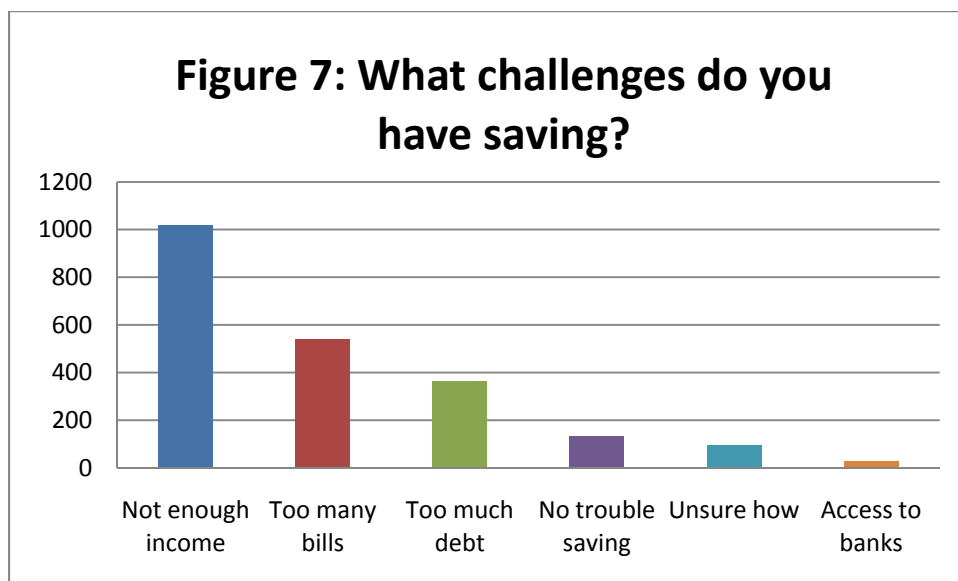


In order to understand the needs of clients, the survey asked what bills cause the most trouble or are most difficult for families (see Figure 6). More than a quarter of clients answered that credit card bills

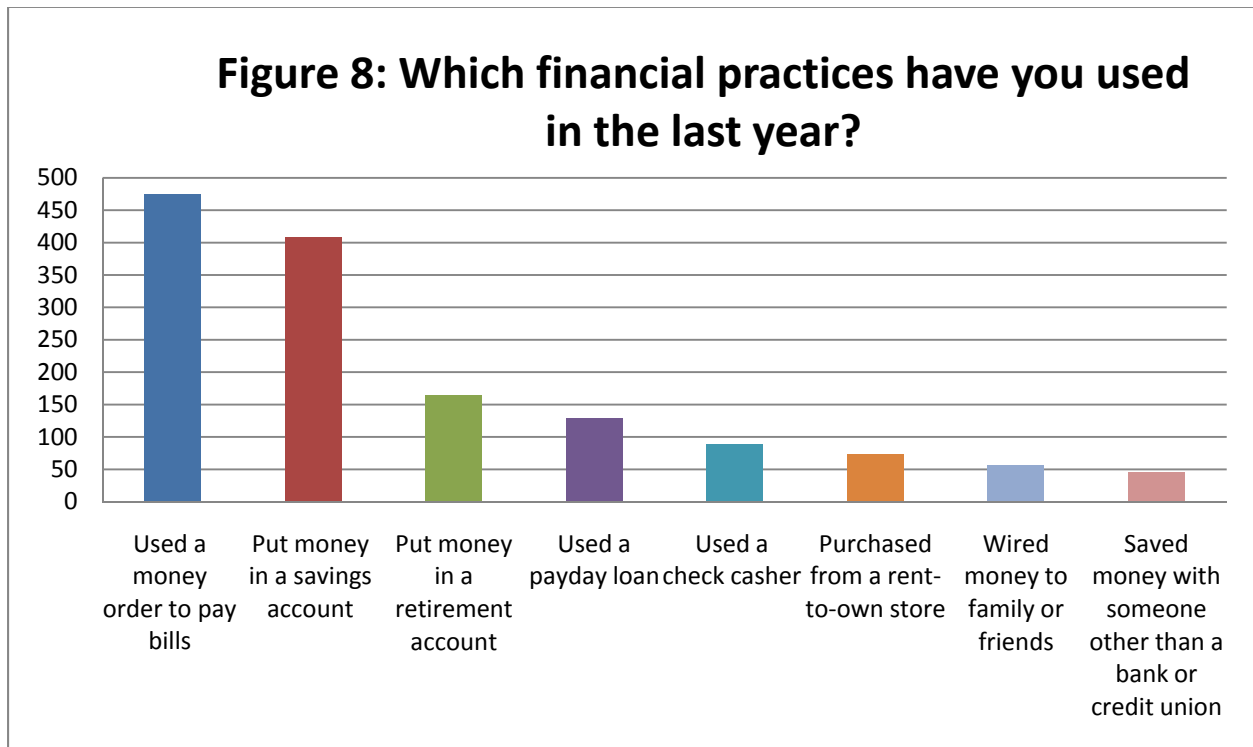
were problematic, while covering basic living needs like food and clothing were nearly 20 percent of responses. Utility bills, housing issues, and health costs were also problematic for clients. In previous years, housing costs were the largest response from clients.



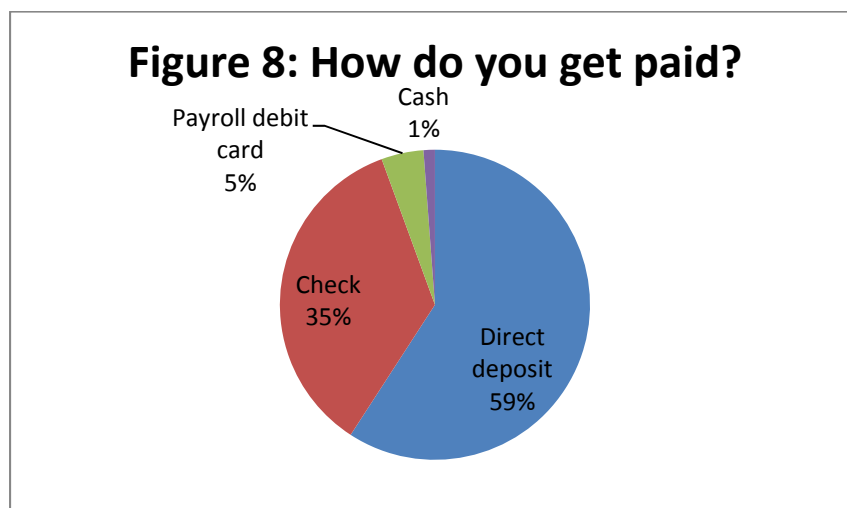
Most clients reported difficulties in earning enough money to meet their basic needs, making saving money difficult (see Figure 7). More than 1,000 clients (225 more than last year) indicated they did not earn enough money to save. Other clients expressed that they had too many bills and too much debt to save. Contrary to previous reports on low-income families and asset building, few clients felt that they did not know the best ways to save or that they lacked the financial products to do so.



As in previous years, most clients are banked in some fashion and participate in savings products (see Figure 8). However, more than 450 clients used money orders to pay bills while hundreds of other clients reported using payday loans, check cashers, and rent-to-own stores.

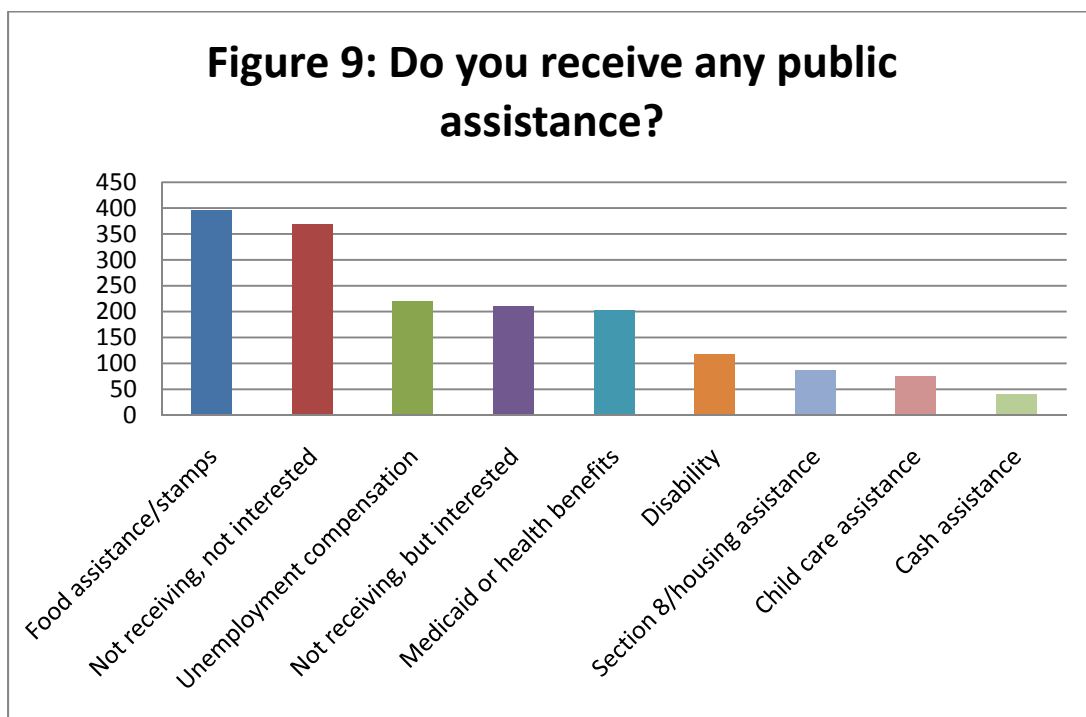


The survey also reveals that most clients are paid through direct deposit into their bank accounts, which means they are eligible for quicker refunds from the IRS when they e-file (see Figure 9). Very few clients reported being paid in cash (15) but some did report not being paid consistently (247).



The survey also asked about client participation in other public assistance and government programs (see Figure 9). For the second year in a row, the numbers receiving public assistance were elevated.

More than 375 clients answered they received food stamps or assistance while nearly 200 indicated they received a form of health assistance. An increased number of clients also indicated they received unemployment compensation (more than 200) or disability assistance (more than 100). This increase in assistance claims could represent more clients being eligible for programs than before due to reductions in their income or in awareness of the programs. It is also likely that promotion by 211/First Call for Help and the Ohio Benefit Bank added to increased public benefit claims. The continued recession also is a likely contributor to the number of unemployment compensation claims. Unemployment compensation and disability payments do not count as “earned income” and cannot be used to claim the EITC.



Demographics

The survey asked a series of demographic questions to understand the clientele (see Table 4). The Coalition continues to primarily serve African American clients (67%) and some Caucasian clients (18%). The Coalition now serves more Hispanic clients than in previous years, some 9% of the total. Females continue to represent a larger share of clients than males. Education levels and experiences of clients continue to vary but most clients have at least a high school education and some higher education experience but not a completed degree.

More than half of clients are renters but thirty-one percent own their home. An increasing amount of clients are in group settings such as living with family and friends, dorm, or group setting. The average income for a client was \$21,650, though many reported being unemployed or offered incomplete salary information. The average was 44, consistent with previous years. More than 200

clients reported being either evicted or part of a home foreclosure suggesting possible future partnerships with housing groups.

	Client Response	Percentage
Race		
• White/Caucasian	265	18%
• African American	981	67%
• Hispanic	126	9%
• Asian	54	4%
• Other/Mixed	31	2%
Gender		
• Female	879	64%
• Male	490	36%
Education Level		
• Less than High School	127	9%
• High School/GED	502	35%
• Some College/Technical School	472	33%
• Two-Year Degree	134	9%
• Four-Year Degree	98	7%
• Some Graduate Education	93	7%
Home Ownership		
• Rent	697	55%
• Own	331	26%
• Own with no mortgage	69	5%
• Live with friends or family (doubling-up)	169	13%
• Dorm/group setting	15	1%

Recommendations

There are a variety of ways that the Coalition and overall VITA efforts can be strengthened but they require stable and likely increased funding and stronger partnerships with financial institutions and social service groups.

Funding

The Cuyahoga Coalition is primarily funded by the Board of Cuyahoga County Commissioners through a federal re-grant of the Temporary Aid to Needy Families program (TANF). This allocation makes sense given the focus of the EITC is to provide assistance to families with children. Recently, the United Way of Greater Cleveland provided financial support to the Coalition, as well as marketing and outreach services. Under a new IRS grant program, the Coalition receives support for technology and site management. However, much of the money is designated for expanding the Coalition's operations into "hard-to-reach" areas, additional counties, and suburbs. More funding is needed for basic operations including site managers, outreach, marketing materials, and staff. Some funding suggestions include:

- The federal government should increase its allocation to the IRS VITA grant program, which is currently at \$12 million for all the free tax coalitions in the country. The grant process could also be improved, as grantees do not know their status until very close to the beginning of tax season.
- While the State of Ohio provides support for the Ohio Benefit Bank, which offers free tax preparation with a volunteer or coach, there is no state-level support for Ohio's VITA programs. Only funding the OBB is insufficient to help the thousands of Ohioans who need tax assistance and qualify for the EITC. The OBB is also not funded at a high level and requires private donations and foundation support. Currently, 27 other states provide fiscal support through grants and discretionary funding for asset building, EITC, and free tax programs.

Increases to federal and state funding would help bring more EITC dollars to families and communities while increasing the number of properly prepared and filed tax returns to the IRS and Ohio Department of Taxation.

Outreach/Marketing

The Coalition's marketing efforts remain strong but more can be done to reach filers who use paid tax preparation or do not file. Beginning in the fall, families should hear about free tax services and be encouraged to not take out costly loans from paid preparers. Schools, religious institutions, libraries, and labor unions can play a pivotal role in this outreach to their membership. Many of these groups work with the Coalition but more can be done such as speaking events, mailers, newsletter inserts, pay-stub inserts, robo-calling, and inserts with W-2 forms. Some other specific marketing suggestions include:

- The radio is still a popular way to reach low-income families. Specifically, working women tend to prefer the radio as a medium for information and entertainment. Over the last two years, clients increasingly reported hearing radio ads about free tax preparation and the EITC.
- Increasing outreach to the Latino and Asian communities is an important part of growing as a Coalition. There are a substantial number of low- and moderate-income families who are Hispanic and could utilize this service. Developing materials in Spanish, which the Coalition has done, is a good first step. Also, making particular outreach efforts through city council representation, libraries, and ward clubs in those areas would be a logical and easy outreach step.
- Using “tear-off” sheets for potential clients so they have the ability to call 2-1-1 at their leisure and pass a tangible piece of marketing material to others. The paid preparation chains use this as an effective recruitment method.

Services

- While most clients are banked, a small portion would like to open bank accounts. Having a bank presence at larger sites, offering first accounts and short-term, safe savings products, would allow clients to get more from their tax preparation experience.
- Many clients use alternative or “fringe banking” services that drain money from their paychecks and the local economy. The Coalition should develop or work with other groups to hand out information about the large fees and interest from check cashers, pawn shops, payday lenders, and rent-to-own stores.
- The largest use of refunds is to pay utility bills. There are several utility assistance programs, specifically around gas and electric bills, that could help many clients in the low-income range.
- The Ohio Benefit Bank provides a unique analysis of government benefit eligibility that could provide referrals to the Coalition (or vice versa) to strengthen the financial stability of families. Some VITA sites use OBB software but many are not set-up to do so. The Coalition should ask about clients’ benefit eligibility, current claims, and interest in learning more. This is particularly critical given the rise in public assistance claims by clients who use the Coalition for free tax preparation.
- Certified housing and income counselors, and community credit counseling services should play a larger role in helping clients who want to save but need some products, plans, or goal-setting assistance. Some sites have more participation in this area than others but each site could offer a call-back or follow-up option for these services. The key remains connecting the services and products for families, making the process as easy as possible.

POLICY MATTERS OHIO IS A NON-PROFIT, NON-PARTISAN RESEARCH INSTITUTE DEDICATED TO RESEARCHING AN ECONOMY THAT WORKS FOR ALL IN OHIO. POLICY MATTERS SEEKS TO BROADEN DEBATE ABOUT ECONOMIC POLICY BY PROVIDING RESEARCH ON ISSUES THAT MATTER TO OHIO'S WORKING PEOPLE AND THEIR FAMILIES. AREAS OF INQUIRY FOR POLICY MATTERS INCLUDE WORK, WAGES, AND BENEFITS; EDUCATION; ECONOMIC DEVELOPMENT; ENERGY POLICY; AND TAX POLICY. GENEROUS FUNDING COMES FROM THE FORD, JOYCE, GUND, CLEVELAND, PUBLIC WELFARE, ANNIE E. CASEY, SISTERS OF CHARITY AND W.K. KELLOGG FOUNDATIONS, THE ECONOMIC POLICY INSTITUTE, AND GREATER CLEVELAND COMMUNITY SHARES. TO THOSE WHO WANT A MORE FAIR AND PROSPEROUS ECONOMY... **POLICY MATTERS**.

MAIN OFFICE: 3631 PERKINS AVENUE, SUITE 4C-E • CLEVELAND, OHIO 44114

COLUMBUS: 300 E. BROAD STREET, SUITE 490 • COLUMBUS, OHIO 43215

[HTTP://WWW.POLICYMATTERSOHIO.ORG/](http://www.policymattersohio.org/)



© 2011 Policy Matters Ohio. Permission to reproduce this report is granted provided that credit is given to Policy Matters Ohio. All rights reserved.