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The Minimum Wage Alternative No One Is Talking About

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August 25, 2016

Lawmakers and activists have often touted the minimum wage as a way to address poverty, but one tax break could provide an alternative that is less economically risky.

The Earned Income Tax Credit (EITC) is a tax break aimed specifically at lower income households. It helps the working poor by allowing them to keep more of their paycheck when paying income tax. Some experts note the policy could help the poor while avoiding many of the economic shortfalls that the minimum wage faces.

"I think that the EITC is a better way to help the working poor than increasing the minimum wage," American Enterprise Institute Scholar Michael Strain told InsideSources. "The minimum wage runs the risk of reducing employment among low-wage workers whereas the EITC has been shown to actually increase employment among low wage workers."

Employers face an increased cost in labor when the minimum wage goes up. They often have few options to offset the added expenditures besides reducing their workforce or increasing prices. The EITC, however, doesn't increase labor costs because it doesn't change what a worker gets paid, only what they take home after taxes.

"One, its a way to make the tax code more progressive, and two, it does so with relatively fewer distortions to the economy than, say, a policy like the minimum wage," Tax Foundation Federal Projects Director Kyle Pomerleau told InsideSources. "It doesn't mess with the employer side, its something that the employee gets."

Economic Policy Institute Budget Analyst Hunter Blair believes the credit shouldn't be used to replace the minimum wage. He notes the credit is powerful on its own but should be used in conjunction with the minimum wage rather than as a potential replacement.

"It is a very good program on its own," Blair told InsideSources. "There are also significant complementaries with the minimum wage, and so it can be more beneficial in conjunction with an increase of the minimum wage."

Cato Institute Scholar Chris Edwards warns there is a lot of misinformation when it comes to the credit. He notes that the credit in practice functions more like a government subsidy as opposed to a tax break. Many people on the program get a larger credit than they actually paid in taxes.

“The Earned Income Tax Credit is mainly a spending program, it is not a tax cut program,” Edwards told InsideSources. “Its always talked about as a tax cut but its not, its a welfare spending program that’s run through the tax code.”

Many households that are eligible for the credit don’t have to pay any income taxes at all. Essentially, if a person is eligible for a $5,000 credit but they only paid $2,000 in income taxes, they will have a negative $3,000 tax liability. The government makes up the different and pays them that $3,000.

“I think the problem is too many Republicans see it as a better policy than an increase in the minimum wage but that doesn’t mean its a good policy,” Edwards also noted. “Its politically favorable to both parties to talk about it as a tax cut. There is clearly a political incentive to talk about it as a tax cut.”

Those in support admit that the credit has been used as a welfare spending program. Nevertheless they note even with the refundable negative tax credit, it is still a better policy for addressing poverty. Blair adds lower income workers still face other taxes and expenditures the program helps offset too.

“You certainly get the refundable portion of it but that’s important because a lot of these lower income households pay payroll taxes as well,” Blair stated. “The EITC is helping them offset the payroll taxes that might be taxing them into poverty.”

The Internal Revenue Service calculates that as of 2014 there were 27.5 million people receiving benefits through the program. The IRS estimated in 2015 recipients got $69 billion in tax credits. Edwards estimates that 88 percent of all benefits for that year were the result of spending.