The Dual Origins of the Earned Income Tax Credit: Theorizing Indirect Assistance at the Subnational Level

Context: Existing theories of indirect assistance derive from a significant transformation of the U.S. welfare state at the federal level—the growth of the Earned Income Tax Credit (EITC) between the 1970s and 1990s as welfare declined—and point to 3 reasons for this transformation including cost-cutting, the policy design advantages of indirect assistance, and the U.S. cultural valuation of work over welfare. While these theories help to explain the growth of the EITC at the federal level, these theories do not encompass the growth of indirect assistance at the state level, where the EITC's pattern of growth departs significantly from that of the federal credit.

While nearly 3 out of 5 states had adopted their own EITCs by 2020 (Williams 2019), some states had adopted EITCs in the early 1980s long before the federal EITC's major expansion in the early 1990s while some states adopted their EITCs in 2010 or later, long after the end of federal welfare entitlement in the mid-1990s through PRWORA and the redesign of state welfare systems (Williams 2019). The state-level EITCs also vary in terms of generosity and structure with some providing substantial resources to lower income households and others providing only providing a pittance (Williams 2019). The patterns of EITC adoption and growth at the state level indicate a more complex story about how the EITC became a core component of the U.S. welfare state, which this paper begins to explore through an in-depth case of the first state-level EITC.

Existing explanations have not been able to fully explain the EITC's growth at the federal level (Ventry 2000; Bertram 2015; McCabe 2018) and the patterns of growth at the state level also call to question the three most prominent explanations of the EITC's growth. The first explanation suggests the EITC allowed for cost cutting while obscuring the distributional effects of reducing more universal programs – governments restructure assistance to a smaller part of the poor population and thwart backlash to retrenchment by moving assistance into the tax system (Myles and Pierson 1997). This explanation does not encompass the continued growth of tax credit programs providing cash assistance to low-income households after the curbing of more expansive social commitments (i.e., welfare rights) in the mid-1990s (McCabe 2018), and also does not fully explain the turn to the EITC in fits and starts at the subnational level. The EITC's inconsistent growth at the subnational level among historically high-spending states challenges the theory that it was an obvious form of restructuring for more generous policymakers faced with austerity (Myles and Pierson 1997).

Another perspective argues that the policy design of the EITC, and other tax credits has led to their growth. Various features of indirect assistance—including programmatic ambiguity, more favorable institutional pathways, and invisibility as spending in a period of austerity—contribute to the success of tax credit programs (Howard 1997, Steensland 2008, McCabe 2018). Other scholars have questioned the extent to which these programs are invisible or ambiguous for policymakers at the federal level (Ventry 2000) and variation in the take up and growth at the state level also complicates this explanation, under which greater uniformity between states might be expected if the various advantageous features drove the turn to indirect assistance.

A third perspective suggests that the EITC's growth is best explained by cultural values that demand a different approach to addressing poverty than offered by the old AFDC system. The EITC is thus a way of reducing poverty more aligned with the nation's "pro-work ethos" in which the least advantaged households receive the supports they need to participate in the labor market—the culturally approved way to exit poverty and experience social mobility (Howard 1997; Ventry 2000; Halpern-Meekin et al. 2015). At the federal level, this explanation cannot account for why the EITC is both too thin and too incomplete to eliminate in-work poverty or facilitate social mobility (Alstott 2010; Nichols and Rothstein 2015), and state variation is also left unexplained by this perspective since the pro-work ethos should permeate across states and lead to a more uniform EITC adoption.

Empirical Intervention: This paper sheds new light onto the dynamics of the U.S.'s turn to indirect assistance through an in-depth case study of EITC adoption and development in Wisconsin; this paper then compares this case with the trajectory of the EITC at the federal level. Wisconsin was an early adopter of the EITC, and state policymakers first began discussing a state-level EITC in 1979, well before the federal EITC grew in prominence. My research finds that Wisconsin first turned to the EITC as part of a larger plan to reinvigorate its economy through the creation of a tax-based welfare system, similar to the Negative Income Tax proposals of the 1970s, and that through the 1990s the EITC remained a core component of liberal visions for restructuring the welfare state, which liberal Democrats hoped would be a springboard for a new comprehensive system of social protection to replace the much maligned AFDC system. In Wisconsin, policymakers engaged in active debates about the merits and demerits of the EITC as public policy in terms of poverty reduction, labor market participation, and tax equity during the 1980s and 1990s, indicating that the EITC was visible to policymakers and that the multiple meanings the EITC took in distributive politics reflected the political struggle about the future of the welfare state. This trajectory stands in contrast to the dominant account of the federal credit in which Southern Democrats advanced the EITC in the 1970s in order to derail guaranteed income schemes, and the credit then grew almost by happenstance as significant tax legislation created opportunities in which the EITC increased tax equity and both parties had claim to supporting the "working poor" (Howard 1997; Myles and Pierson 1997).

The comparison of the EITC's trajectory in Wisconsin and at the federal level illuminates the program's relationship to the demise of welfare protections. In Wisconsin, Liberal Democrats made a substantial expansion of the state's EITC a prerequisite for embarking upon the redesign of the state's welfare system in the 1990s, and this agreement would reshape the state's welfare politics. By prioritizing the EITC's growth, liberal Democrats forewent the possibility of using their political leverage to ensure protections for households without work. Over the course of the 1990s liberal Democrats in Wisconsin would try to enact a more comprehensive system but failed to do so and instead the state adopted a strict workfare system. Conservative actors used the EITC to mask the true effects of this workfare system, presenting a punitive system as a supportive jobs program. Liberal Democrats attempted to gain ground on creating a more protective system of income maintenance over the course of almost two decades to find that EITC expansion better supported conservative aims than their own. These events stand in contrast to what is known about the federal EITC's growth and development which some scholars have presented as having a fairly neutral relationship to welfare's demise (Howard 1997; McCabe 2018) and other scholars have presented as a concession for the end of universal protections (Myles and Pierson 1997).

Finally, this paper examines the way in which Wisconsin's EITC informed the growth and development of the federal EITC, treating Wisconsin as a dual origin point for understanding the EITC's significance in the U.S. welfare state and welfare politics. Wisconsin's EITC influenced federal policymakers' decisions around EITC expansion, and federal policymakers even altered the structure of the federal EITC to mimic the Wisconsin structure, which was more generous for larger families. Federal policymakers' ideas about the role of the EITC in reducing poverty also appear to originate in Wisconsin. The way in which Wisconsin redesigned its welfare system in the 1990s heavily shaped national welfare discourse, making the end of entitlement through PRWORA appear possible to federal policymakers, and also became a model for other states post-PRWORA. This paper argues that the Wisconsin EITC was a progenitor for the contemporary federal EITC and thus is an important case for understanding the EITC welfare regime.

Theoretical Contributions: This paper makes three theoretical contributions through the comparison of the Wisconsin and federal EITC trajectories. First, it introduces a new explanation for the growth of indirect assistance, arguing that liberal restructuring efforts and conservative retrenchment efforts drive the growth of indirect assistance, as liberals attempt to formulate a comprehensive system under austerity and conservatives required a means to hide the redistributive harms of their policies. Second, the paper respecifies existing theories, for instance arguing that the ambiguity and invisibility of indirect assistance limited liberals ability to realize more protective welfare restructuring. Third, the paper underscores the importance of subnational policymaking in the growth of indirect assistance, drawing attention to role of states in the ascendancy of this form of distributive policy. More generally, it shows the way in which the study of state-level policymaking in the U.S. context can illuminate the most important forces and dynamics shaping politics and policy.

Works Cited

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