Financial Literacy Can Unlock the Anti-Poverty Potential in the Earned Income Tax Credit

By William Pereira

American democracy offers equality of opportunity, and the American economy is supposed to limit inequality of outcomes. In practice, neither holds evenly. In 1982, the first year the Forbes 400 was compiled, the group's combined net worth was $93 billion. In 2025, it was $6.6 trillion — up roughly 7,000% in just over four decades. Median U.S. household income, by contrast, rose only 270% over the same period.

Meanwhile, the poverty rate has barely budged: the Supplemental Poverty Measure was 12.9% in 2024, virtually unchanged from 12.3% in 1975. As of 2025, the poverty line stood at $32,150 in annual income for a family of four.

No conspiracy produced this combination of soaring wealth at the top, stagnation in the middle and persistent poverty at the bottom. It's the predictable result of an economy that rewards higher-order talent and automates away commodity-like work — a trend artificial intelligence is likely to accelerate. As a society, we should work to minimize inequality without distorting the market system that remains our best engine of innovation and opportunity. With nearly $90,000 of GDP per capita, any American willing and able to work should be able to provide a decent living for a family.

The usual remedies — more education, a higher minimum wage, income redistribution — all have real drawbacks. Even excellent public education is unevenly available, and not everyone can apply skills the modern economy rewards. Raising the minimum wage will likely reduce employment. And redistribution schemes, like a universal basic income, risk robbing work of its meaning.

The tax code, of all places, offers a tool that can fight poverty without discouraging work: the Earned Income Tax Credit. In 2024, 24 million taxpayers earning an average of $30,000 received EITC payments averaging roughly $2,900 — the IRS effectively handed one-time payments worth about 10% of income to roughly 7% of the U.S. population. Payments phase out gradually as wages rise, with no cliff: an increase in wages always produces a net gain in income. For a married couple filing jointly, the credit phases out at $69,000.

In theory, a $70 billion annual cash transfer to low-wage workers should meaningfully cut the poverty rate. It hasn't. The EITC has lifted many individual families out of poverty, but it hasn't moved the national poverty rate. Our experience preparing returns for lower-income taxpayers suggests why — and what to do about it.

Cash transfers under the EITC are necessary, but not sufficient. Alongside the money, we need to teach recipients what to do with it: how to save, invest and avoid common financial errors. The EITC is one side of the coin; financial literacy is the other, equally necessary, side.

That literacy can be delivered in several ways. Volunteers preparing returns under the IRS's Volunteer Income Tax Assistance (VITA) program could spend thirty minutes with each client after filing, discussing how they'll save, spend or invest their refund. Schools, from elementary through community college, can build financial literacy into their curricula. Employers can tie it to 401(k) matches or benefit discounts, and lenders can tie it to interest-rate or fee reductions on mortgages and auto loans.

Smarter timing and defaults would help too. Distributing refunds and credits in monthly installments, rather than one annual lump sum, would slow spending and encourage saving — and eliminate the high-interest loans many low-income filers take out to bridge the three-week gap between filing and refund.

Cash transfers could also default into IRAs, HSAs, 529 plans or debt-reduction plans, with recipients free to opt out but better off if they simply do nothing.

Finally, twenty percent of eligible workers don't claim the EITC at all, leaving nearly $17 billion in cash transfers unclaimed each year. Better marketing — through social media influencers, employers and VITA preparers — could meaningfully lift uptake.

As a VITA tax preparer, I have seen firsthand what a $2,900 inflow can do for someone earning $30,000 a year — and I have seen that potential squandered for lack of financial know-how. A sustained, focused effort to expand financial literacy among lower-income taxpayers could finally let the EITC do what it was designed to do: bend the poverty curve down.

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