The TCJA and the Child Tax Credit

The Tax Cuts and Jobs Act (TCJA) provided good news for families for the coming Tax Year 2018. The TCJA doubled the credit amount, increased the refundable portion, and extended its capacity to include dependents other than qualified children. In addition, the TCJA widened the group of taxpayers eligible for the credit by considerably increasing the adjusted gross income (AGI) phaseout scope. These changes are effective for tax years 2018 through 2025.

HIGHER PHASEOUT SCOPE

Under the TCJA, a taxpayer's possible credit amount begins to level out at $400,000 of modified AGI (MAGI) for joint filers and $200,000 for all others. These amounts are not adjusted for inflation. In 2017, the credit began to phase out at $110,000 for joint filers, $55,000 for married filing separately, and $75,000 for all others. The distinction for married filing separately no longer exists, and the threshold for joint filers nearly quadrupled (for others, the threshold rose by 166%).

The AGI is the same unless a taxpayer is a resident of Puerto Rico, Guam, American Samoa, or the Northern Mariana Islands or has any foreign earned income and/or housing costs that he or she elected to exclude from gross income under Sec. 911. Thus, making is unwise to take the foreign earned income exclusion. The credit amount decreases by $50 for every approximate $1,000 by which the taxpayer's MAGI exceeds the threshold amount.

HIGHER CREDIT AMOUNT

The TCJA eliminated dependency exemptions for tax years 2018 through 2025 but assisting families with the additional credit. The revised child tax credit doubles the credit amount from $1,000 to $2,000 per "qualifying child." The credit amount is not adjusted for inflation. A qualifying child has the same definition as for dependency exemption purposes but must also be under age 17. None of the child tax credits are adjustable per the inflation rate.

The relationship test requires the individual to be the taxpayer's (1) child or a descendant of the child, or (2) sibling or stepsibling or a descendant of the sibling or stepsibling. The residence test requires that the individual have the same principal place of residence as the taxpayer for more than half the year. The support test requires that the individual does not provide more than half of his or her own support for the calendar year in which the tax year of the taxpayer begins. Taxpayers with MAGIs below the threshold will be able to claim a $2,000 credit for each qualifying child. A whopping 100% increase!

OTHER DEPENDENTS COVERAGE

Perhaps the most unanticipated change to the child tax credit is the addition of a $500 credit for each dependent who does not satisfy the definition of a qualifying child. Dependents eligible for the partial credit include "qualifying relatives" for dependency exemption purposes.

A qualifying relative must meet the relationship, gross income, and support tests. The relationship test includes all individuals who meet the qualifying child relationship test, plus the taxpayer's lineal ancestors, stepparents, aunts, uncles, nieces, nephews, certain in-laws, and any individual who lives with the taxpayer and meets the other two tests.

The gross income test requires that the individual's gross income is less than the personal exemption amount. Although that amount becomes zero for tax years 2018 to 2025 for purposes of calculating taxable income, the IRS announced a personal exemption of $4,150 for 2018 (up from $4,050 for 2017). Finally, the support test requires that the taxpayer provides more than half of the individual's support.

The new $500 credit includes not only qualifying relatives but also qualifying children (for purposes of the dependency exemption) who are not eligible for the $2,000 credit because they are age 17 and over. These qualifying children include those ages 17 and 18 (or up through age 23 for full-time students and any age for children who are totally and permanently disabled) and meeting the other tests.

The TCJA modified another change for the eligibility for qualifying children in which a taxpayer identification number (TIN) used to be sufficient, a qualifying child must now have a Social Security number (SSN) for the taxpayer to claim the

$2,000 credit. However, taxpayer can claim a $500 credit for individuals without an SSN, as long as they have a TIN and meet the other dependency tests.

REFUNDABLE CREDIT

A maximum of $1,400 can be refundable of the $2,000 credit per qualifying child. However, $500 credit for other dependents is not refundable. The $1,400 refundable portion is adjusted annually for inflation after 2018. If inflation continues to rise annually, over time, the refundable portion will get closer to the full $2,000 credit, which is not adjusted for inflation. Formerly, the entire maximum credit amount of $1,000 per child could be refundable under certain criteria.

The refundable portion of the credit only applies when the taxpayer is unable to fully use the $2,000 nonrefundable credit to offset his or her tax liability.

IMPACT FOR MIDDLE-INCOME TAXPAYERS

In the past, middle- to high-income taxpayers may have largely ignored the child tax credit. However, the TCJA expanded the credit, both in terms of eligible taxpayers and eligible dependents thus increasing the eligible pool of taxpayers. In addition, the amount of the credit doubled, and the refundable portion boosted by 40%. Beginning with 2018 returns, the child tax credit takes on new importance, especially with the abolition of dependency exemptions.

Questions?

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