Family Tax Provisions and the Child Tax Credit Increases in 2018

The Tax Cuts and Jobs Act (TCJA) of 2017 brought upon U.S. taxpayers the most drastic changes in the tax code in several years. Although politicians called for making the tax return process simpler, they, as usual, are far off the mark. While the discussions to simply the Form 1040 are still in discussion, American families can hope for better news at tax filing time. The U.S. Tax Code is complex and the TCJA did not simplify matters. However, there were changes enacted to help the average family taxpayers.

Taxpayers should remain informed that the personal exemptions have been taken away, but the standard deduction level has increased. In many cases, this can be attractive to tax filers. Another big change in the family provisions of the TCJA is the Child Tax Credit (CTC). These changes allow more American families to take advantage of this credit, which can also be a refundable credit.

Congress has decreased the income threshold allowing for more two-income families to utilize the Child Tax Credit due to the changes in the qualifying requirements. It expanded the child tax credit from $1,000 to $2,000, making *up to* $1,400 refundable, while increasing the income phaseout from $110,000 to $400,000 for married couples. This change in the CTC will be available until 2025, after which the provisions expire.

The standard deduction and exemption changes have an impact on federal revenue and increases the national debt but are important implications for the structure of the individual income tax. The changes of TCJA will simplify the tax code for many Americans. With the standard deduction increasing, the value of itemized deductions is diminished. It is estimated that nearly 29 million more American will be better off taking the increased standard deduction instead of going through the process of itemizing deductions.

Currently, the family tax provisions of the TCJA affects at least six tax provisions, which include the child tax credit, the child and dependent care tax credit and exclusion for employer-sponsored child and dependent care benefits, the earned income tax credit, filing status, the standard deduction, and tax rates and brackets. However, this article will address specifically the child tax credit.

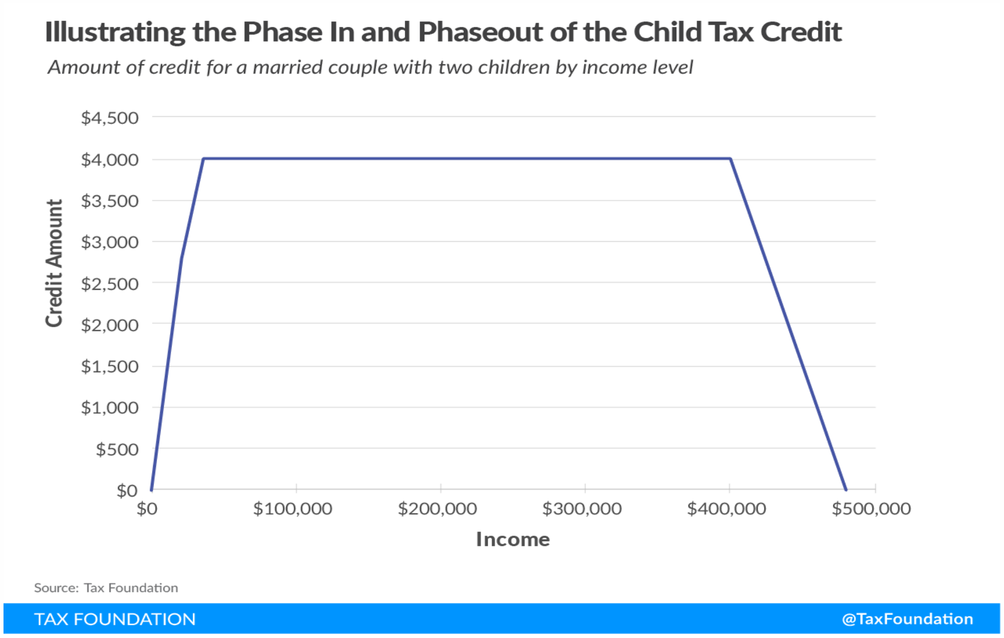
Child Tax Credit

As in past years, the child tax credit provides a tax credit per child under the age of 17 for filing families. If the credit exceeds a taxpayer's liability, they may receive a portion of the credit as a refund, thus creating an attractive refundable credit…even for international tax filers. Eligibility for the credit depends on various criteria, including the age of the child and the income level of the household.

Prior to the tax reform, the child tax credit was a credit which offset tax liability. A separate credit, the Additional Child Tax Credit, allowed for a portion of the child tax credit to be refundable if it exceeded tax liability. However, under the TCJA there will not be an identified *Additional Child Tax Credit* separate from the child tax credit; instead, there is one credit that is refundable. However, it is subject to specific requirements.

The TCJA doubles the maximum child tax credit from $1,000 to $2,000 but only up to $1,400 of the credit is *refundable*. An important note is that the only portion of the child tax credit that is indexed to inflation is the refundability limit. Under current law, if the tax credit exceeds tax liability, taxpayers generally use an earned income formula to determine what is refundable. It would have been 15 percent of income above $2,500, up to the full refundability amount. For example, a family with $5,000 in earned income would be eligible for a refund of $375.

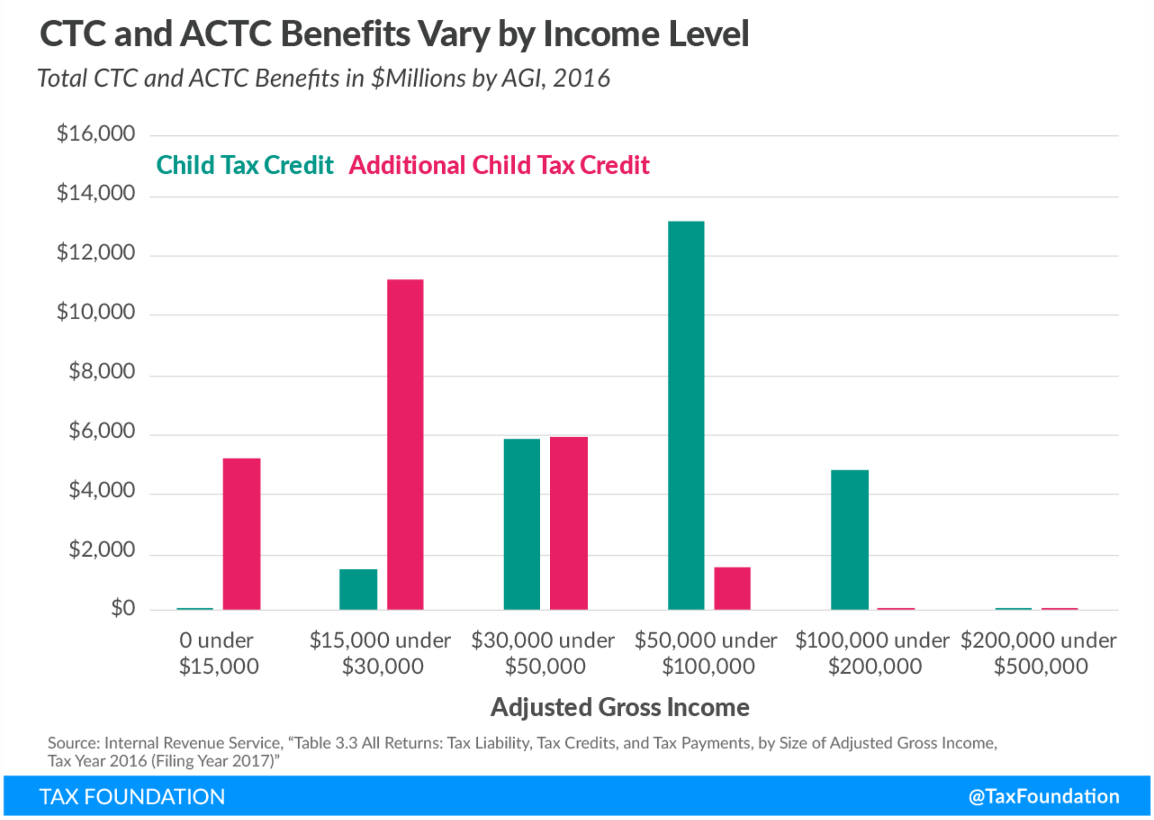
Under the old law, the credits phased out at much lower income levels. Under the TCJA, the credit now phases out at a 5 percent rate for married filers making above $400,000 and all other filers making above $200,000. For example, the maximum credit per child a single filer making $220,000 could receive would be $1,000 instead of the maximum credit of $2,000, as illustrated in the graph.



An added benefit under the TCJA is the expansion of the child tax credit by adding a *nonrefundable* $500 credit for each dependent who is not a qualifying child *under* age 17. Now a qualifying child turning age 17 during the tax year can now provide a tax credit to the filing taxpayers. This new credit, referred to as a “family credit,” has been intended to compensate for the eliminated personal exemption but is subject to the same phaseout as the child tax credit. These expansions of the child tax credit are currently scheduled to expire after 2025 as well.

The Tax Foundation reported that:

In tax year 2016, pre-TCJA, more than 22 million households claimed the child tax credit for a total of $26.8 billion, while 18.9 million claimed the Additional Child Tax Credit for benefits of $25.4 billion. The benefits of the child tax credit peak at households making between $50,000 and $100,000, while the benefits of the Additional Child Tax Credit peak at households making between $15,000 and $30,000. Because of the income phaseout range prior to the TCJA, a relatively small number of households in the $200,000 to $500,000 AGI range benefited from either of the credits.



Standard Deduction & Exemption

The new tax law increases the standard deduction to $12,000 for single filers, $18,000 for heads of household, and $24,000 for joint filers in 2018. The previous standard deductions were $6,500, $9,550, and $13,000 respectively, which sought the need for itemization. TCJA also eliminates the personal exemption, which had allowed households to reduce their taxable income by $4,150 for each filer and dependent. At least three other tax provisions also vary with the taxpayers' filing status: filing status, the standard deduction, and tax rates and brackets.

Generally, taxpayers may file as single, married filing jointly, married filing separately, or head of household. The filing status affects the size of some credits, the amount of the standard deduction, and which tax rates and tax brackets income falls under as illustrated in the table below per the TCJA:

	Unmarried Individuals	Married Individuals Filing Joint Returns	Heads of Households
2018 Standard Deduction	$12,000	$24,000	$18,0000
Rate	Taxable Income Over		
10%	$0	$0	$0
12%	$9,525	$19,050	$13,600
22%	$38,700	$77,400	$51,800
24%	$82,500	$165,000	$82,500
32%	$157,500	$315,000	$157,500
35%	$200,000	$400,000	$200,000
37%	$500,000	$600,000	$500,000

Table: Tax Brackets, Rates, and Standard Deductions 2018
Source: Tax Foundation

An inadvertent effect of the old law is that it created marriage penalties or marriage bonuses, meaning that the combined income tax liability of a married couple would be higher or lower than it would have been if they remained single. The Tax Cuts and Jobs Act condensed marriage penalties and bonuses across the tax brackets, as all tax brackets for married filers are exactly double those for single filers, with the exception for the top 37 percent marginal rate. However, with the marriage penalties or bonuses purged, the lower-income individuals who are filing married will see an increase of the qualifying income for the Earned Income Tax Credit (EITC) into the phaseout range. Thus, creating in a new marriage penalty because of the reduction of the EITC. However, a complete elimination of the marriage penalties and bonuses would require a drastic overhaul of the U.S. income tax system, which would most likely never occur in our lifetimes.

TCJA brought about various many other changes. It is best to try to get educated, ask questions from your tax professionals, and do your research to ensure that you are getting the best breaks available for US tax filers.

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