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INSIGHT

The Child Tax Credit: Temporary Expansion for 2021 Under the American Rescue Plan Act of 2021 (ARPA; P.L. 117-2)

Updated May 12, 2021

In recent years, there has been increased interest in providing direct benefits to families with children to reduce child poverty in the United States, sometimes in the form of tax benefits. The National Academy of Sciences (NAS) included a "child allowance" as part of a package of policies to reduce child poverty over 10 years. (Senator Romney has also proposed a child allowance.) Some research has suggested that increasing the amount of the child tax credit that low-income families receive would substantially reduce child poverty, boost future earnings, and potentially improve future health and education outcomes.

In the 116th Congress, there were several legislative proposals to expand the child tax credit, especially for lower-income families that tend to receive little or no benefit from the current credit. In the 117th Congress, a temporary one-year expansion of the child credit (for 2021) was included in the American Rescue Plan Act of 2021 (ARPA; P.L. 117-2). The Biden Administration has proposed making the full refundability provision included in the ARPA expansion of the child credit permanent, while extending other ARPA provisions through the end of 2025.

This Insight provides a summary of the child tax credit prior to ARPA and an overview of the temporary child credit expansion under ARPA for 2021.

How would the child credit have been calculated in 2021 before ARPA?

For 2021, prior to ARPA, the child tax credit would allow eligible taxpayers to reduce their federal income tax liability by up to $2,000 per qualifying child. A qualifying child was generally any dependent child under 17 years old. The credit was reduced in value, or phased out, by $50 for every $1,000 of income over $200,000 ($400,000 for married couples who file joint tax returns).

If a taxpayer's income tax liability was *less* than the maximum value of the child tax credit, the taxpayer may have been eligible to receive all or part of the difference as a refundable credit. The refundable portion of the child tax credit—the amount which was greater than income taxes owed—is referred to as the additional child tax credit (ACTC) and was calculated using what is sometimes referred to as "the earned income formula." Under the earned income formula, the ACTC gradually increased, or phased in, as earned income rose above $2,500. The maximum amount of the ACTC was $1,400 per qualifying child. CRS estimates that about one in every five taxpayers (19%) with a credit-eligible child had low incomes that resulted in them receiving less than the maximum credit.

After 2021, the ARPA expansion described in this Insight is scheduled to expire, and the credit would thus revert to the "prior law" parameters described above until the end of 2025.

How does the child credit change in 2021 under the American Rescue Plan Act?

The American Rescue Plan Act of 2021 (ARPA; P.L. 117-2) makes several temporary changes (for 2021 only) that expand the child tax credit, primarily for low-income taxpayers. These changes include

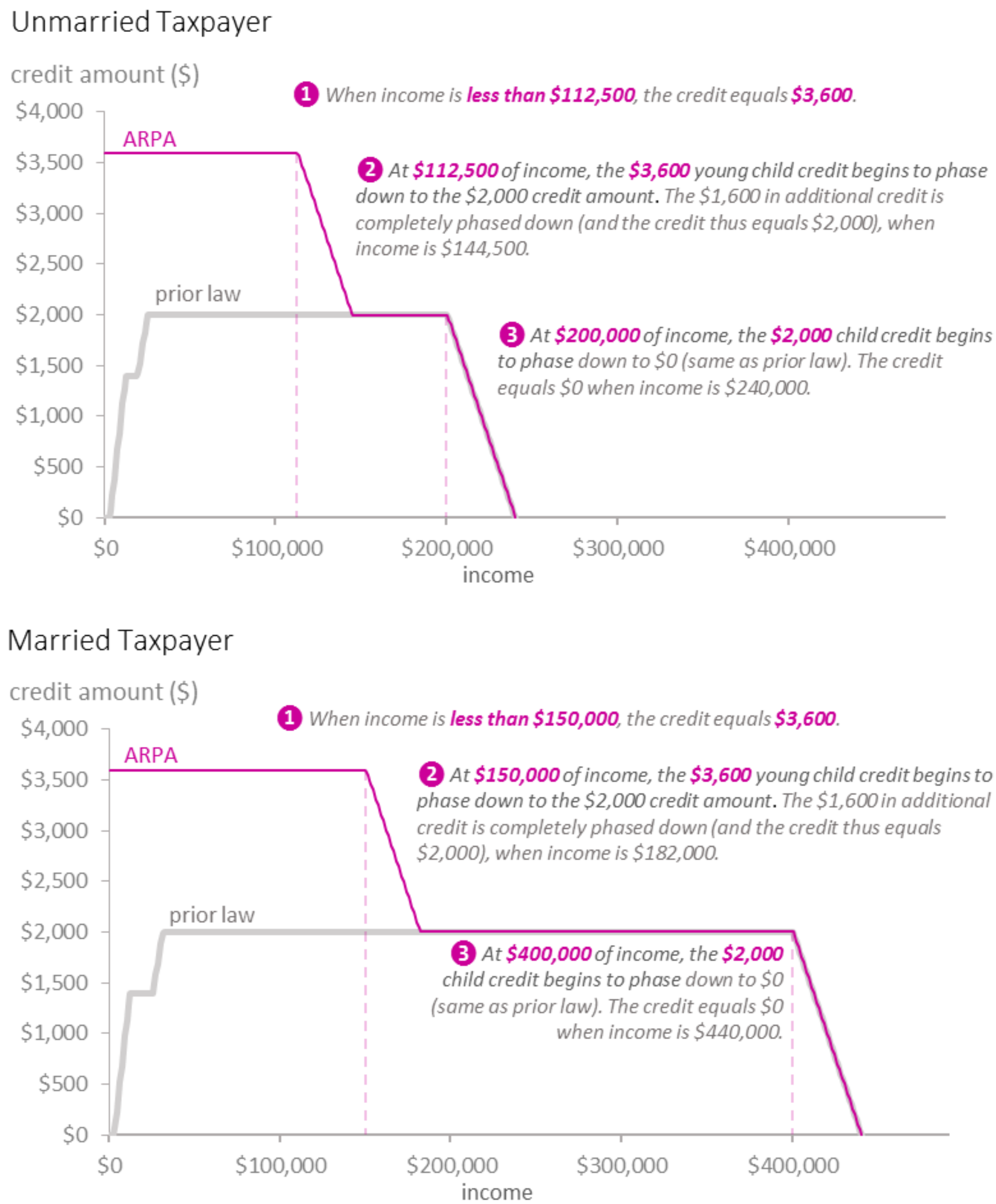
- **Expanding eligibility to 17 year olds:** The law increases the maximum age for an eligible child from 16 to 17.
- **Making the credit fully refundable:** The law eliminates the ACTC phase-in based on earned income and eliminates the ACTC cap of $1,400 per child. Hence, the child credit is "fully refundable" and the full value is available to otherwise eligible taxpayers with no earned income.
- **Increasing the credit for low- and moderate-income taxpayers, with larger increases for younger children:** The law increases the maximum amount of the credit from $2,000 per child to $3,600 per child for a young child (0-5 years old) and $3,000 per child for an older child (6-17 years old), as illustrated in the figures below. Generally, this increase in the maximum child credit of $1,600 per young child and $1,000 per older child gradually phases out at a rate of 5% as income exceeds specified thresholds until the credit amount equals the current-law maximum of $2,000 per child. These thresholds are $75,000 for single filers, $112,500 for head of household filers, and $150,000 for married joint filers. (The actual income level at which the credit phases down to $2,000 per child depends on the number and age of qualifying children.) For many families, the credit then plateaus at its prior-law level of $2,000 per child and phases out when income exceeds the current-law threshold of $200,000 ($400,000 for married joint filers). For larger families, the credit may never plateau at the $2,000 per child level, but simply continue to gradually phase out.

These changes will increase the amount of the credit for low- and moderate-income taxpayers, while higher-income families will generally receive the same benefit as under prior law (unless they have an eligible 17-year-old), as illustrated in the figures below.

The Joint Committee on Taxation estimates this temporary one-year expansion of the child credit would cost $110 billion, mostly in FY2021 and FY2022 (these estimates also include the relatively smaller cost of permanently extending the credit to residents of U.S. territories).

Child Credit Amount for One Young Child (0-5 Years Old) for 2021

Prior Law and the American Rescue Plan Act of 2021 (ARPA; P.L. 117-2)

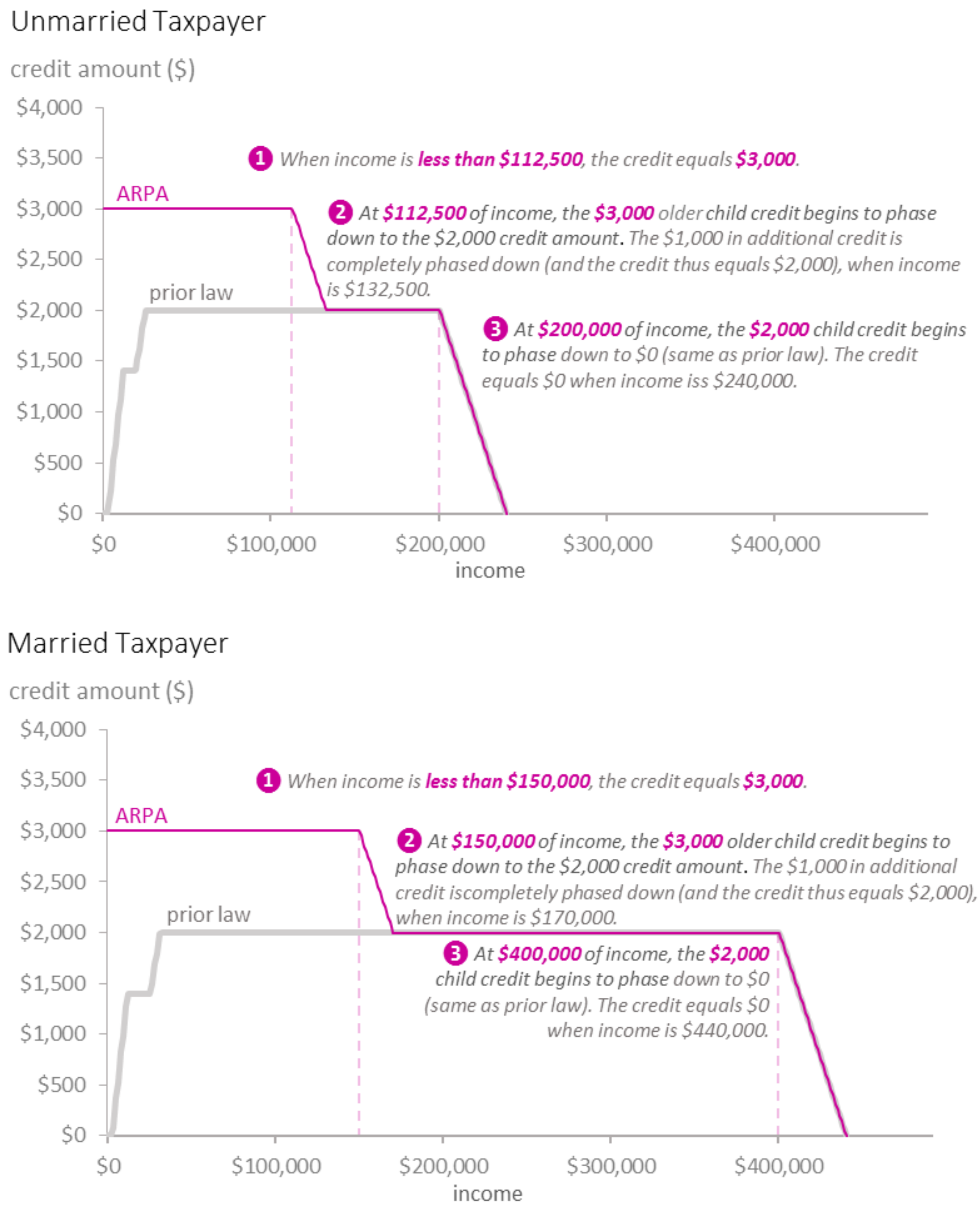


Source: CRS calculations based on IRC §24 and P.L. 117-2.

Note: A stylized example assuming the taxpayer has one qualifying child and all income is earned income, with no other sources of income and no above-the-line deductions claimed. Unmarried taxpayers are assumed to file as head of household, married taxpayers are assumed to file joint returns.

Child Credit Amount for One Older Child (6-17 Years Old) for 2021

Prior Law and the American Rescue Plan Act of 2021 (ARPA; P.L. 117-2)



Source: CRS calculations based on IRC §24 and P.L. 117-2.

Note: A stylized example assuming the taxpayer has one qualifying child and all income is earned income, with no other sources of income and no above-the-line deductions claimed. Unmarried taxpayers are assumed to file as head of household, married taxpayers are assumed to file joint returns.

How does ARPA advance the credit?

ARPA directs the Treasury to issue *half of the expected 2021 credit* in periodic payments beginning after July 1, 2021 (these periodic payments will generally be equal in amount). Taxpayers will claim the remaining half of the total 2021 credit when filing their 2021 income tax return in early 2022. The *expected 2021* credit amount is the total amount the taxpayer would be expected to receive in 2021 (and not just the amount of the credit that exceeds income taxes owed).

The amount of the payments advanced in 2021 are estimated based on 2020 income tax data or, if unavailable, 2019 income tax data. Families can update this information on a portal in 2021.

The IRS can adjust income tax withholding to take into account the advanced child credit.

Will taxpayers need to repay the advanced credit?

When a taxpayer files their 2021 return (in 2022), they will generally first calculate the *total amount* of the 2021 child credit they are eligible for (based on the number of qualifying children, income, and marital status for 2021). Then, the taxpayer will subtract from their total 2021 credit the sum of advanced child credit payments they received during calendar year 2021. For example, if an unmarried taxpayer had two young children and less than $112,500 of income *in 2020 and 2021*, they would be eligible for a total child credit for 2021 of $7,200. Since they would have received half of their total 2021 credit in advanced payments in calendar year 2021 ($3,600), they would ultimately claim the remaining half ($3,600) on their 2021 return. In this case, the taxpayer is not repaying the advanced credit—they are simply splitting their total credit between the advanced payments they received in 2021 (50% of their total credit) and the remaining 50% of the credit they claim on their 2021 tax return.

However, in cases where a taxpayer receives *more in advanced payments* than the total 2021 credit they are eligible for, they will generally need to repay any excess credit. A taxpayer may have excess credit due to changes in income, marital status, or number of qualifying children between the year used to estimate the advance (2020 or 2019) and their actual circumstances in 2021. For example, if a taxpayer's estimated advance payments totaled $5,400 (based on an *estimate* of three qualifying young children) but the total 2021 credit they are actually eligible for is $3,600 (because they only had one qualifying young child), they would need to repay up to $1,800 (the difference between $5,400 and $3,600). Excess payments caused by *changes in the number of qualifying children* generally will not need to be repaid for lower- and moderate-income taxpayers who are protected by a safe harbor (this safe harbor decreases as income rises). Repayment may either reduce a taxpayer's 2021 tax refund or result in the taxpayer being required to remit payment to the IRS (or be subject to offset of a future tax refund).

Below are two illustrative examples of how much in excess advanced child credit an unmarried taxpayer would need to pay in certain circumstances.

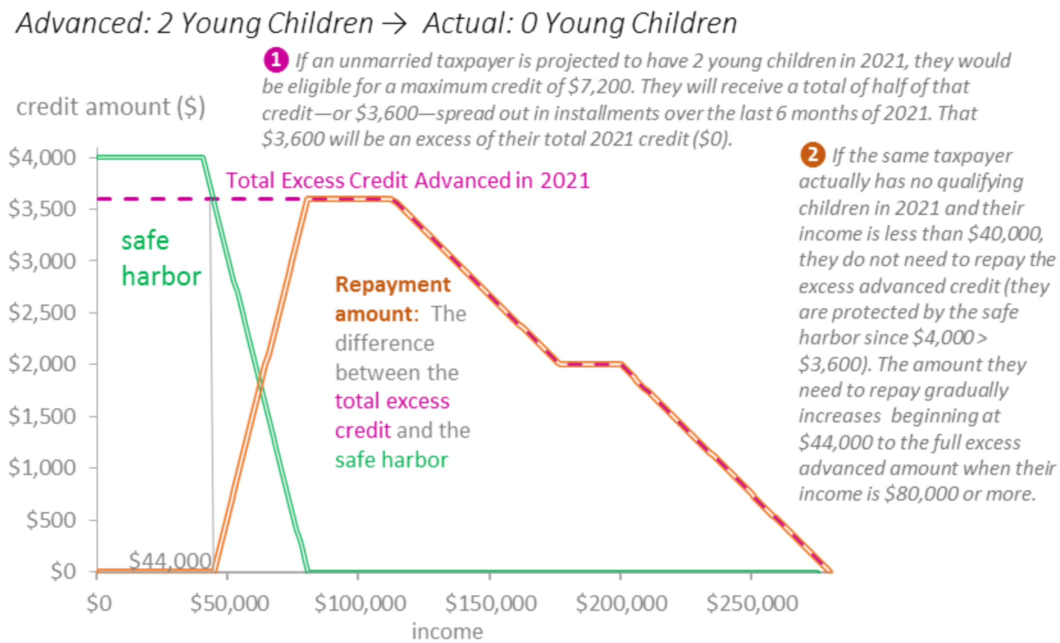
Steps for Reconciling Advanced Payments of the Child Credit with the Actual Credit on 2021 Tax Returns Under the American Rescue Plan Act of 2021 (ARPA; P.L. 117-2) That Occur Due to an Incorrect Number of Qualifying Children

Steps to Reconcile Excess Advanced Payments of the 2021 Child Credit	Example 1 **Single parent with 2 qualifying young children in 2020 and 1 young child/0 older children in 2021**	Example 2 Single parent with 2 qualifying young children in 2020 and 0 qualifying children in 2021
Step 1: Determine "excess" credit. A. Calculate **the total credit** the taxpayer is eligible for on their 2021 return. B. Calculate the **amount they were advanced** in 2021 (based on 2020 information). C. Subtract the advance **(B)** from the total they are actually eligible for **(A).** If **B** is greater than **A**, the taxpayer will have received an **excess credit** (the difference between A and B). In cases where the taxpayer has received an **excess credit**, the taxpayer may need to repay some or all of the excess **(continue on the steps below)**.	For example: If the taxpayer's income is under $112,500 (in 2020 and 2021), then: A. Total 2021 credit: **$3,600** B. Amount advanced: **$3,600** (50% of $7,200) C. Excess credit: $0 (=$3,600-$3,600) The difference between the actual credit they are eligible for in 2021 and the advanced credit is $0. The taxpayer will effectively not receive a credit when they file their 2021 return, because they already received it as the advanced credit.	For example: If the taxpayer's income is under $112,500 (in 2020 and 2021), then: A. Total 2021 credit: **$0** B. Amount advanced: **$3,600** (50% of $7,200) C. Excess credit: **$3,600**
Step 2. Determine maximum safe harbor amount. A. Determine net difference between: (i) Number of qualifying children used to determine *advanced credit* and (ii) number eligible for *actual credit* in 2021. B. Multiply **(A)** by $2,000.	Not applicable, no excess payment.	A. The net difference between the (i) number of qualifying children from a 2020 tax return (2 children) used to determine the advanced credit and (ii) the number of children claimed on a 2021 tax return (0 children) is **2 children**. B. $2\ children\ x\ \$2{,}000 = \$4{,}000$
Step 3: Phaseout maximum safe harbor, if applicable. Depending on **income** and **filing status in 2021**, the maximum safe harbor may be subject to reduction. Safe harbor reduced ratably (i.e., proportionally) between: **$40,000-$80,000** single filers **$50,000-$100,000** head of household filers **$60,000-$120,000** married joint filers	Not applicable, no excess payment.	**No phaseout**: If a single person in 2021 (i.e. single filer in 2021) has income under $40,000, their safe harbor is not reduced (i.e., it equals the **maximum safe harbor amount**). **Phaseout:** If a single person in 2021 has income between $40,000 and $80,000, the maximum safe harbor phases out ratably in relation to income in the phaseout range. For example, if income were **$60,000** in 2021, the maximum safe harbor would be reduced by: $\left[\frac{\$60{,}000-\$40{,}000}{\$80{,}000-\$40{,}000}\right]=$**50%** A **$4,000** safe harbor **reduced by 50%** would equal **$2,000.** **No safe harbor:** If a single person in 2021 has **more than $80,000** in income, their safe harbor amount is **$0**.
Step 4: Calculate the amount of any excess credit that needs to be recaptured (or paid back) on 2021 tax return: Subtract the **safe harbor** amount (determined after step 3) from the total amount of **excess credit** (determined in step 1) in 2021. If the **safe harbor amount** is **greater than or equal to excess payment**, none of the advanced amount needs to be paid back.	Not applicable, no excess payment.	If income in 2021 for a single person is: **Under $44,000:** Payback amount is **$0** since the excess credit of **$3,600** is less than the **$4,000 safe harbor** when income is under $40,000. Between $40,000 and $44,000 the safe harbor gradually declines but is still greater than or equal to $3,600. **$44,000+:** Payback amount equals **$3,600 excess credit** *minus* **safe harbor** until income is $80,000 or more at which point the total excess credit of $3,600 needs to be repaid. *If income was $60,000, the* ***safe harbor*** *would be* ***$2,000****, the single person would need to pay back* ***$3,600*** *-* ***$2,000*** *or* ***$1,600*** with their 2021 tax return. *If income was $80,000 or more, the* ***safe harbor*** *would be* ***$0****, the single person would need to pay back all* ***$3,600*** *in excess credit with their 2021 return.*

Sources: CRS analysis of P.L. 117-2.
Notes: Assumes advanced payment that would be received in 2021 would be based on 2020 income and family structure (number of qualifying children and marital status). Broadly, income is assumed to be the same between 2020 and 2021 to isolate the impact of a changing number of qualifying children.

Repayment of Excess Advanced Child Credit for Children Incorrectly Claimed Under the American Rescue Plan Act of 2021 (ARPA; P.L. 117-2)

Unmarried Taxpayer, 2021



Source: CRS calculations based on IRC §24 and P.L. 117-2.

Notes: Stylized example assuming advanced amount based on projection that taxpayer has two young children in 2021. In actuality, the taxayer has no young children. The taxpayer has no other qualifying children. An unmarried taxpayer with no children is assumed to file as single.

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