

The Federal Child Tax Credit

What is the federal child tax credit?

Parents may claim a credit against federal income tax equal to \$1,000 for each child under age 17. The credit was enacted in the Tax Relief Act of 1997 (TRA) and first allowed in 1998. It was made permanent by the American Taxpayer Relief Act (ATRA) of 2012.

Are there income limitations?

The credit is reduced by \$50 for every \$1,000 of income over \$110,000 of adjusted gross income for married joint filers and \$75,000 for head of household filers. A married couple filing jointly with two children under age 17 will become ineligible for the credit when their income exceeds \$149,000; a single parent claiming the credit for one child will become ineligible when income exceeds \$94,000.

Is the credit refundable?

The child credit is partly refundable; the refundable portion is referred to as the “additional child tax credit.” The additional child tax credit equals the greater of:

- 15 percent of earned income over \$3,000, or,
- for families with three or more children, payroll taxes in excess of the federal earned income tax credit.

For example, a married couple with two children under age 17 and \$40,000 of income is eligible for \$2,000 in child tax credits, \$1,000 for each child. If the couple claims the standard deduction, their federal income tax will equal \$1,120 in 2016. They use \$1,120 of their \$2,000 credit to reduce their liability to \$0. They may claim up to 15 percent of their earnings in excess of \$3,000 as a refund. Assuming all \$40,000 of their income is from wages, that means they would be eligible to claim up to \$5,550 of the remaining credit as a refund (15 percent of \$40,000, minus \$3,000, equals \$5,550). The result is that they claim \$1,120 as an offset to their tax liability and are paid the remaining \$880 as a refund.

How much do Minnesotans claim?

In tax year 2014, 412,510 federal income tax returns filed by Minnesotans claimed \$554 million in the nonrefundable portion of the federal child credit. The average amount claimed was \$1,342. For the same year, 237,490 returns filed by Minnesotans claimed \$325 million under the refundable additional child credit. Some of these returns also claimed the nonrefundable portion of the credit. The average additional child tax credit (the refundable portion) was \$1,366.

How does Minnesota compare with other states?

Nationwide, 15.1 percent of all income tax returns claimed the child credit, compared with 15.4 percent in Minnesota. The average amount of the nonrefundable portion claimed nationwide was \$1,211, compared with \$1,342 in Minnesota. Since the credit is only partly refundable, the larger average amount claimed on Minnesota returns may result from Minnesotans having above-average incomes, and consequently more federal liability available to be offset by the child credit. Utah had the highest average nonrefundable portion, at \$1,533, and the District of Columbia had the lowest, at \$959.

The average amount of the refundable portion claimed nationwide was \$1,343, compared with \$1,366 in Minnesota. Utah had the highest average refundable portion, at \$1,619, and Massachusetts had the lowest, at \$1,180.

How has the credit amount changed over time?

The credit equaled \$400 per child in 1998, increased to \$500 in 1999, \$600 in 2001 and 2002, and \$1,000 beginning in 2003. The \$1,000 credit amount was made permanent in 2012 by ATRA.

Has the credit always been refundable?

When first enacted in TRA, the child credit was only refundable for taxpayers with three or more children, and only to the extent that their payroll taxes exceeded the federal earned income tax credit. The implicit rationale was that the refundable portion of the federal earned income tax credit was first used to offset payroll taxes for Social Security and Medicare, and then any payroll taxes left over after the federal earned income tax credit could be offset by the federal child credit. This refund mechanism was limited to families with three or more children because families with fewer children and no federal tax liability would typically have all of their payroll taxes offset by the federal earned income tax credit and none left over to be offset by the new child credit.

In 2001 the refundable portion was changed to be the greater of:

- 15 percent of earned income over a minimum amount for all families regardless of the number of children, or,
- for families with three or more children, payroll taxes in excess of the federal earned income tax credit (the provision that was already in law).

The 2001 law set the minimum amount at \$10,000 and provided for it to increase annually for inflation; ATRA made the \$10,000 as indexed for inflation permanent. The American Recovery and Reinvestment Act of 2009 temporarily reduced the indexed \$10,000 to \$3,000, not adjusted for inflation, for tax years 2009 and 2010 only; ATRA extended the \$3,000 minimum amount through 2017. The Protecting Americans from Tax Hikes Act of 2015 made the \$3,000 minimum amount permanent.

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