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Michelle Freeman

East Tennessee State University, freemanms@etsu.edu

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The Expanded Child Tax Credit and Advance Payments: What Your Clients Need to Know

By *Michelle Freeman, Ed.D., CPA*

The American Rescue Plan, signed into law on March 11, 2021, contained \$1.9 trillion of relief for taxpayers (Segers, 2021). The new law, with several retroactive 2020 tax return items, passed in the middle of filing season. Tax preparers scrambled to quickly understand how to process the remaining tax returns and how to handle the millions of already filed tax returns. Tax professionals and individuals seem to now have a handle on the changes that were retroactive, but the 2021 expanded Child Tax Credit and its advance payments are still causing much confusion among individual taxpayers. Tax preparers need to be able to explain this credit to their clients.

What is the expanded Child Tax Credit?

Although the Child Tax Credit has been available to taxpayers for a long time, the expanded Child Tax Credit allows for more children to qualify due to three main factors. First, a qualifying child's maximum age of eligibility increased from 16 to 17. Second, the amount of credit allowed per child increased. Previously, the credit was worth \$2,000 per child. With the American Rescue Plan, the credit is worth \$3,600 for children aged 5 and under and \$3,000 for children aged 6 through 17 at the end of the tax year. Third, the refundable portion of the credit increased. Before the new law, if the taxpayer had no taxable income only \$1,400 was refundable; however, now the credit is fully refundable even at \$0 taxable income (Looking ahead: How the American Rescue Plan affects 2021 taxes, part 2, 2021). Taxpayers should not confuse this credit with the \$500 credit for other dependents, which is still not refundable, and there are no advance payments of this credit (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic D: Calculation of Advance Child Tax Credit Payments, 2021).

Are there limitations on eligibility due to income?

Taxpayer income may preclude the taxpayer from receiving the Child Tax Credit. The maximum credit is allowed for taxpayers up to the following modified adjusted gross income limits: single and married filing separately at \$75,000; head of household at \$112,500; and married filing jointly and qualifying widows at \$150,000.

After these amounts are reached, the credits begin to phase out in two parts. The credit is split into its original \$2,000 amount and the new amounts of \$1,600 for children 5 and under or \$1,000 for children ages 6 through 17. The additional credits of \$1,600 or \$1,000 are reduced by \$50 for every \$1,000 above the modified adjusted gross income limits above. The original \$2,000 credit from previous years is reduced by \$50 for every \$1,000 above the modified adjusted gross income if the modified adjusted gross income is more than \$400,000 for married filing jointly returns and \$200,000 for all others. (Looking ahead: How the American Rescue Plan affects 2021 taxes, part 2, 2021).

What are advance Child Tax Credit payments?

For the tax year 2021 only, advance payments of the expanded credit are also allowed so that taxpayers do not have to wait until their tax returns are prepared to receive the benefit of this tax relief. They are not taxable income but advances of the credit. According to the IRS, advance payments can be up to "50 percent of the estimated amount of the Child Tax Credit that you may properly claim on your 2021 tax return during the 2022 filing season" (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic A: General Information | Internal Revenue Service, 2021). As an example, if taxpayers do not have income limitations and meet the other requirements, they should receive a monthly

check or direct deposit of \$300 per child aged 5 and under and \$250 per child aged 6 through 17 at the end of the year.

Who qualifies for advance Child Tax Credit payments?

Taxpayers with a qualifying child and with a “main home in one of the 50 states or District of Columbia for more than half the year” qualify for the advance Child Tax Credit payments (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic B: Eligibility for Advance Child Tax Credit Payments and the 2021 Child Tax Credit, 2021). The tests for a qualifying child have only changed in terms of the age of the dependent, as discussed previously. If the qualifying dependent was alive at all in 2021 and lived with the taxpayer for more than half the time that the child was alive in 2021, then the child qualifies for the 2021 Child Tax Credit and the advance payments (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic B: Eligibility for Advance Child Tax Credit Payments and the 2021 Child Tax Credit, 2021). U.S. military stationed outside the United States on active duty are considered to have a main home in the United States (Looking ahead: How the American Rescue Plan affects 2021 taxes, part 2, 2021).

When will taxpayers receive monthly advance payments?

Taxpayers will see advance payments either by check or direct deposit to their bank accounts on July 15, Aug. 13, Sept. 15, Oct. 15, Nov. 15 and Dec. 15 (People who don't have to file taxes may need to register for monthly advance child tax credit payments, 2021). They may also receive a letter from the IRS stating they are eligible and the amount they should receive. (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic A: General Information, 2021). If an eligible taxpayer does not receive the advance payment around the dates discussed above, they can track their payment. The payment cannot be tracked until it is more than five days past the direct deposit date, four weeks past the date of mailing, six weeks past date of mailing if mail is being forwarded and nine weeks past payment date if the address is a foreign address. Taxpayers should complete Form 3911 Taxpayer Statement Regarding Refund to start a trace and mail to the appropriate address in the instructions for the form (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic B: Eligibility for Advance Child Tax Credit Payments and the 2021 Child Tax Credit, 2021).

What can taxpayers do to see if they are eligible?

Taxpayers can easily check to see if they are eligible to receive advance payments of the expanded Child Tax Credit by going to the following website: <https://www.irs.gov/credits-deductions/advance-child-tax-credit-eligibility-assistant> (Advance Child Tax Credit Eligibility Assistant, 2021). They will need to have their 2020 tax return while checking eligibility (or 2019 tax return if they have not filed 2020).

As a matter of curiosity, I tried out this tool to see how easy or difficult it was to maneuver. The website proved fairly simple to navigate. The first question asked whether I had previously claimed the credit and if I planned to claim the credit for 2021. The second question asked if I had lived in

the U.S. for over 50 percent of the year. It then asked for my filing status and 2020 modified adjusted gross income as well as the number of children I had aged 5 and under on Dec. 31, 2021, and aged 6 to 17 on Dec. 31, 2021. The calculator then displayed the following results:

You may receive half of the Child Tax Credit for each child in equal payments each month for the remainder of 2021. Payments will start in July.

- For each qualifying child under age 6, you will receive up to \$1,800 in advance, generally paid in six monthly payments of \$300.
- For each qualifying child aged 6 through 17, you will receive up to \$1,500 in advance, generally paid in six monthly payments of \$250.

These advance payment amounts begin to be reduced if your modified AGI exceeds:

- \$150,000 if married and filing a joint return or if filing as a qualifying widow or widower
- \$112,500 if filing as head of household
- \$75,000 if you are a single filer or are married and filing a separate return

The site further gave me the ability to manage the payments I would receive by clicking on a series of links that would take me to the Child Tax Credit Update Portal where I could click on another button labeled “Manage Advance Payments.” After clicking that button, I was directed to sign in with my IRS ID or to create an ID with the ID.me website. Reluctantly, I went through the stages of creating this ID, which required pictures of my driver's license, phone number, a video selfie and my Social Security number. Once my ID was verified, I was admitted into the portal where I could change my bank account information, see what payments had been processed and also choose to unenroll from advance payments. Out of curiosity, I clicked on “processed payments” because I happened to be testing this on the first payment date of July 15. It showed that one payment for \$250 had been processed for me on July 15.

Throughout the second half of 2021, the IRS plans to update the Child Tax Credit Update Portal to allow taxpayers to update their addresses, change the number of qualifying children due to birth or adoption, report a change in marital status, and report a change in income (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic F: Updating Your Child Tax Credit Information During 2021).

What do taxpayers do to ensure they receive payments?

If taxpayers filed their 2019 or 2020 tax returns, they do not have to do anything to receive the payments. If taxpayers did not file a 2019 or 2020 tax return, they will need to use the IRS Non-filer Sign-up Tool. Some non-filers may have already used this tool last year to register for Economic Impact Payments. This website allows eligible taxpayers who do not usually have to file taxes to input information such as name, address, email, date of birth, Social Security numbers for taxpayers and qualifying children aged 17 and under, and bank account information so the IRS can calculate and issue advance Child Tax Credit payments. It will also ask for information about direct deposit bank information. Users of

this tool will usually be low-to-no income families (People who don't have to file taxes may need to register for monthly advance child tax credit payments, 2021). They should use this tool if they have qualifying children born before 2021, are not required to file or did not file a 2019 or 2020 tax return and if they have a main home in the United States for more than half the year (Child Tax Credit Non-filer Sign-up Tool, 2021).

Estimations

Advance payments are determined by estimating the amount of the Child Tax Credit the taxpayer will claim on the 2021 tax return based on what was filed on the 2020 tax return or 2019 if 2020 has not been filed (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic D: Calculation of Advance Child Tax Credit Payments, 2021). Half of the estimated 2021 Child Tax Credit will then be divided by six and paid out in monthly advance payments. For children aged 5 or under, the \$3,600 is divided in half, and the \$1,800 is then split into six payments of \$300 each. For children aged 6 to 17, the \$3,000 is divided in half, and the \$1,500 is then split into six payments of \$250 each (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic D: Calculation of Advance Child Tax Credit Payments, 2021). If the estimation is based on the 2019 tax return because the 2020 tax return has not been processed and then later the 2020 tax return is processed, payments may be recalculated and remaining payments may differ as a result (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic E: Advance Payment Process of the Child Tax Credit, 2021).

Are there potential problems for tax preparers' clients?

There are some potential problems and/or misconceptions about the advance payments. First, taxpayers must realize that the payments are advance payments of a credit that would go against their 2021 tax calculation. If they receive these payments in advance, then only half of the credit remains to net against the tax due on the 2021 tax return, resulting in less offset or refund when they file their 2021 tax returns.

Second, it is possible that the amount of the advance payments could be estimated and paid at a higher amount than the taxpayer is entitled. For example, if their taxable income has increased on the 2021 tax return as compared to 2020 or 2019 (that the calculation was based on) and that increase is above the thresholds, then the taxpayer may owe money back. Also, if their estimated children aged out of the credit or moved out of their household, then the taxpayer may owe money back.

Third, it is also possible that the taxpayer is not the one entitled to the Child Tax Credit for the tax year 2021. For example, many divorced couples have joint custody and alternate years for claiming their children as dependents. If 2021 is not the taxpayer's tax year for claiming the child, but they did claim the child on the 2020 tax return, they will receive advance Child Tax Credit payments for a child they will not claim on the 2021 tax return. They will have to pay those amounts back when they file (Cohn, 2021).

Although repayment protection is offered in some situations, if the taxpayer has any of the above or other concerns, they may choose to unenroll in the advance payments. They will use the Child Tax Credit Update Portal, which was discussed previously, to unenroll (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic A: General Information, 2021). Taxpayers only have to unenroll one time, not each month. Individuals who file married filing jointly must both unenroll. "If one does and the other does not, then the spouse who did not unenroll will receive half of the joint payment" (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic J: Unenrolling from Advance Payments, 2021). Also, in order to stop payments, the taxpayer "must unenroll 3 days before the first Thursday of next month by 11:59 p.m. Eastern Time" (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic J: Unenrolling from Advance Payments, 2021).

How will differences between estimations and actual calculations be handled?

When the taxpayer files their 2021 taxes, they will compare the Child Tax Credit advance payments received to the calculated Child Tax Credit on the 2021 tax return. If the amount of the credit exceeds the amount of the payments received, the taxpayer will claim the remaining amount on the 2021 tax return. However, if the amount received in payments exceeds the amount calculated on the 2021 tax return, the taxpayer may have to repay the excess payment (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic H: Reconciling Your Advance Child Tax Credit Payments on Your 2021 Tax Return, 2021). Taxpayers will receive a letter from the IRS (Letter 6419) in January 2022. This letter will confirm the advance payments made to the taxpayer, and the taxpayer should put it with their tax records so they can input the amount received correctly on their tax calculations.

If the comparison of advance payments to the calculation of the credit shows that excess payments were made, the taxpayer may qualify for repayment protection. Repayment protection provisions are as follows if the main home was in the United States for more than half the year and if modified AGI for 2021 is at or below the following amounts: married filing jointly or qualifying widow at \$60,000; head of household at \$50,000; and single or married filing separately at \$40,000. If the modified AGI exceeds these amounts or the main home was not in the U.S. for over half the year, then the taxpayer's repayment protection may be limited. Repayment protection is completely phased out for the following modified AGI amounts: married filing jointly at \$120,000; head of household at \$100,000; and single or married filing separately at \$80,000.

If the taxpayer meets the qualifications for full repayment protection, the repayment protection is calculated as \$2,000 multiplied by the number of qualifying children the IRS considered to estimate advance payments minus the number of qualifying children used in calculating the credit on the 2021 tax return. If the taxpayer income falls between the limits for full protection and no protection, the amount of protection is calculated as \$2,000 multiplied by the number of qualifying children the IRS considered to estimate advance

payments minus the number of qualifying children used in calculating the credit on the 2021 tax return multiplied by the percentage difference between actual modified AGI and the applicable modified AGI threshold. The IRS offers the following example:


Example: You filed a joint return with your spouse for tax year 2020 and properly claimed the Child Tax Credit for three qualifying children. The IRS estimated your total advance Child Tax Credit payment amount based on these qualifying children. However, when you file your 2021 joint tax return with a modified AGI of \$75,000, you claim the Child Tax Credit for only one qualifying child - and therefore have two excess qualifying children. Your modified AGI of \$75,000 exceeds your applicable \$60,000 modified AGI threshold by 25 percent. Your potential full repayment protection amount of \$4,000 (that is, \$2,000 for each excess qualifying child) is reduced by 25 percent to \$3,000. (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic H: Reconciling Your Advance Child Tax Credit Payments on Your 2021 Tax Return, 2021).

Many taxpayers who find themselves repaying excess payments will do so simply through a reduction of the federal income tax refund. However, it is possible that the taxpayer could end up making payments, and the IRS will work with those to make payment plans.

Potential scams

New initiatives such as this credit and advance payments are a playground for potential scammers. The IRS has issued warnings that plead with all taxpayers to be aware of “scam artists trying to use advance Child Tax Credit payments as a cover for schemes to steal personal information and money” (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic A: General Information, 2021). The IRS further emphasized that they do not contact by email, text or social media to request personal or financial data, and they will not leave messages on answering machines threatening lawsuits or arrests or ask for payments with gift cards (Cohn 2021). They state that taxpayers should beware of “email attachments or links claiming to have special information about advance Child Tax Credit payments or refunds of the Child Tax Credit” (2021 Child Tax Credit and Advance Child Tax Credit Payments - Topic A: General Information, 2021).

Conclusion

The Center on Budget and Policy Priorities did an analysis that stated the expanded “Child Tax Credit could raise four million children out of poverty” (Segers, 2021). Unfortunately, the credit and its benefits are least understood by the families that are in this situation. Tax preparers should consider these issues for their clients and also how they can help the public understand these new rules. 

ABOUT THE AUTHOR

Michelle S. Freeman, Ed.D., CPA is an associate professor at East Tennessee State University in Johnson City, Tenn. She may be contacted at freemanms@etsu.edu.

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