Free markets. Real solutions.

December 2023

R Sheet On

The Federal Child Tax Credit

A Bipartisan Solution That Reduces Poverty and Encourages Employment

Background

The Biden administration and the Republican-controlled House of Representatives are engaged in end-of-the-year negotiations (that could drag on into January) about final tweaks to the U.S. tax code. Republicans want to cut taxes to promote research and development and capital investments to spur job creation, while the White House wants to restore pandemic-era expansions of the federal Child Tax Credit (CTC) to battle poverty.

"If Congress is going to bring back tax cuts for big corporations, it should restore the Child Tax Credit that helped cut child poverty nearly in half," an administration official told *The Hill* in early December. Congress created the CTC in 1997 to provide working parents with a tax credit for each child. The bipartisan legislation emphasized the word "working," but the Biden administration temporarily ended the work requirement (called "refundability") in 2021 during the pandemic. The 2021 update also expanded the size of the credit from $2,000 to $3,600 per child.

The American Rescue Plan, the Biden administration's $1.9 trillion stimulus package passed in 2021, included CTC extensions that expired at the end of 2021, but the debate continues about how to adjust the credit going forward. The disagreement centers on the credit's work requirements, which require annual family earnings of at least $24,000 to receive the full credit. Sen. Joe Manchin (D-W.Va.), a swing vote in an evenly divided Senate, derailed his party's effort to make permanent the program's expansions out of concern that it would promote welfarism rather than work.

Another vocal supporter of work requirements, Sen. Marco Rubio (R-Fla.) told National Public Radio in September that, "If you turn it into just simply a transfer payment, you've absolutely gutted the tax credit concept." The law was passed, he said, to help "working people to keep more of the money they earn in order to raise their children, which is the most important investment we're making in our country." He supports boosting the size of the credit, however, and called on Congress to look at other programs to help American parents who are not working.

There is also debate over costs, given the 2021 expansion is estimated to have cost the U.S. Department of Treasury $180 billion. However, lowering the income threshold at which the credit phases out—currently $200,000 for a single filer and $400,000 for a couple—could reduce cost concerns.

Supporters of the administration's plan point to studies showing that child poverty decreased significantly because of the credit. The U.S. Census' Supplemental Poverty Rate showed that child-poverty rates more than doubled—from 5.2 percent

Summary

- Congress created the Child Tax Credit in 1997 to help working families with kids stay out of poverty.
- During the pandemic, the Biden administration increased the size of the credit and eliminated the requirement that recipients are working.
- After the CTC's expansion expired, child-poverty rates increased.
- The president and Republicans in Congress are debating whether and how to expand the program, with the main battle centering on work requirements.

to 12.4 percent—after CTC expansions expired at the end of 2022. They believe this program is a proven means to battle poverty and hunger. But the lines of contention might not be as insurmountable as they seem—and it is not mutually exclusive to provide cuts for business investment and people with children.

Current Debate

As with all congressional debates, the publicly drawn lines in the sand do not tell the full story in that there might be a compromise solution that addresses both sides' concerns. An R Street Institute study from February 2023 looks at the three main options on the table. **The first option**, favored by Republicans, increases the size of the current tax credit but still restricts it to those who are working. **The second option**, favored by Democrats, makes permanent the temporary pandemic-era changes by expanding the size of the credit and making it available to everyone, working or not.

A third option offers a blueprint for a bipartisan deal. In essence, it is a hybrid that makes some CTC benefits available to non-workers and then phases in additional benefits as earnings increase. This involves adjusting income thresholds and benefit phase-in periods. Some economists have argued that as many as 1.5 million working parents would exit the labor force if the federal government permanently eliminated CTC's work requirements, but this study found "only a small work disincentive." There is also the caveat that the 2021 changes occurred during the pandemic, "when labor supply and labor demand were abnormal and other economic impact payments were given out; people may have reacted differently under more normal circumstances," the study added.

R Street researchers have also proposed a middle-ground solution that could, for example, "provide $2,000 in CTC benefits for everyone and another $2,000 that phase in for workers." Specifically, this third option would reduce child poverty by nearly the same rate as the second option while also minimizing any dis-employment effects. It is a solution that could reduce poverty rates and even encourage employment.

Action Items

R Street encourages members of Congress to seek a hybrid solution that gets beyond the debates that pit corporations against the poor. Congress and the administration can embrace pro-growth tax policies that encourage business investment as well as tax policies that reduce child poverty. Likewise, they can adjust the CTC in a way that helps the neediest children and their parents while including incentives to encourage work, which remains the best anti-poverty measure. This is an issue that needs members of Congress to spend more time working on a compromise rather than soundbites that present the matter as an either-or proposition. A bipartisan approach is particularly useful as the Tax Cuts and Jobs Act is set to expire in 2025.

As with all congressional debates, the publicly drawn lines in the sand do not tell the full story in that there might be a compromise solution that addresses both sides' concerns.

OPTION 1

OPTION 2

OPTION 3

Contact Us

For more information on this subject, contact:
1411 K Street NW
Suite 900
Washington, D.C. 20005
(202) 525-5717
www.rstreet.org

Steven Greenhut
Director, Western Region
sgreenhut@rstreet.org
(909) 260-9836

Ryan Crow
Director, Policy Operations
rcrow@rstreet.org
(202) 525-5717