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"Fixing" What Wasn't Broken: Why Biden's Child Tax Credit Scheme Is a Recipe for Failure

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KEY FINDINGS

The new Biden Tax Credit scheme...

CLOSELY RESEMBLES WELFARE.

DISCOURAGES WORK.

SENDS "FUN MONEY" TO THE FINANCIALLY SECURE.

REWARDS STAYING HOME.

WILL HURT FAMILIES AT TAX TIME.

HAS FAILED BEFORE.

THE BOTTOM LINE:

CONGRESS SHOULD END THE BIDEN TAX CREDIT SCHEME.

Biden radically changed the Child Tax Credit

Prior to the passage of the American Rescue Plan (ARP) in March 2021, American families were eligible for the Child Tax Credit, which was most recently revised by the Trump tax cuts (Tax Cuts and Jobs Act of 2017).[1] However, following the implementation of the ARP, the Child Tax Credit program significantly changed.[2] Credits were hiked, the maximum age for qualifying kids was increased, and, perhaps most importantly, part of the credit is now being distributed in monthly payments, rather than as a lump sum.[3]

On the surface, some of these changes might seem generous or helpful. But a look under the hood quickly reveals these changes will actually do more harm than good.

Instead of providing a break for working Americans, the Biden Child Tax Credit scheme will simultaneously discourage work while actually helping the financially well-off. In short, the Biden administration—and their willing partners in Congress—took a fine system that was easy to understand and reliable and broke it. They transformed it instead into a **poorly designed set of monthly payments containing backwards incentives, fatal flaws, and administrative nightmares**.

HOW IT WORKS: ELIGIBILITY FOR THE CHILD TAX CREDIT

	THE OLD WAY	THE NEW WAY
QUALIFYING DEPENDENT	Up to 16 years old	Up to 17 years old
AMOUNT OF CREDIT	$2,000 per dependent	$3,600 for dependents under six; $3,000 for dependents ages six through 16
REFUNDABLE LIMIT	15 percent refundable, up to a maximum of $1,400 per dependent	Fully refundable
PHASEOUT THRESHOLDS	$400,000 for married filers and $200,000 for all other filers	Reduced to a $2,000 credit starting at $150,000 for married filers, $112,500 for heads of household, and $75,000 for single filers. Reduced further to zero starting at $400,000 for married filers and $200,000 for all other filers
DISTRIBUTION	Lump sum at tax time	50 percent distributed in monthly payments from July through December 2021; 50 percent distributed as a lump sum at tax time

Source: Congressional Research Service

Six major problems with the Biden Child Tax Credit scheme

The new Biden Child Tax Credit scheme is riddled with bad incentives, unintended consequences, and a leap towards more welfare. It prioritizes monthly cash checks to the financially secure over real support for the most vulnerable. And it sets up truly needy Americans to be hit with a massive tax liability come tax time.

One of the worst aspects of the new Biden system is its impact on incentives. Fundamentally, the credit now encourages choosing not to work by rewarding Americans who opt to stay home. The Biden Child Tax Credit scheme is a thinly veiled attempt to increase dependency nationwide.

1 THE BIDEN CHILD TAX CREDIT SCHEME CLOSELY RESEMBLES WELFARE.

An overarching problem with the Biden Child Tax Credit scheme is how it transforms the credits to more closely resemble welfare-style payments.

Typically, tax credits are added together as part of a lump sum refund—or subtracted from taxpayers' liability—during tax season. This is a once-per-year process and, by keeping these payments within the context of a tax return, it is clearer to taxpayers that these dollars are a "discount" on taxes they already (hopefully) paid through working and earning a living.

But the Biden Child Tax Credit scheme seeks to change this and normalize the flow of regular, monthly checks to the middle class—even though they would not typically receive government checks of this kind.

By having checks arrive in mailboxes and checking accounts on a rolling basis, the tax credits more closely resemble monthly welfare programs like food stamps or cash welfare (TANF), which are also distributed on a monthly basis. In fact, the smallest possible child tax credit for a family of three is now larger than the maximum possible cash welfare benefit for that very same family.[4]

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The monthly allotments also disconnect the payments from the tax return process and will create a sense of expectation—or dependency—on the part of recipients.

Making matters worse, these payments are now going to middle-class Americans, a population typically ineligible for welfare benefits.

And, to help make the transformation to a welfare-style system complete, the credits have also been redesigned in a way that discourages work—and are now fully accessible, even if Americans do not work at all.

2 THE BIDEN CHILD TAX CREDIT SCHEME DISCOURAGES WORK.

Under the new Biden Child Tax Credit scheme, a typical family with two kids under six will receive $7,200 per year—not counting the value of other government benefits they might be eligible for.[5] In fact, when coupled with other welfare and unemployment benefits, **the new monthly payments of the Biden Child Tax Credit scheme create a disincentive to work for many Americans.** In some instances, it is the factor that makes the welfare-versus-work tradeoff a reality.

A TYPICAL FAMILY WITH TWO KIDS UNDER SIX WILL RECEIVE $7,200 PER YEAR IN PAYMENTS.

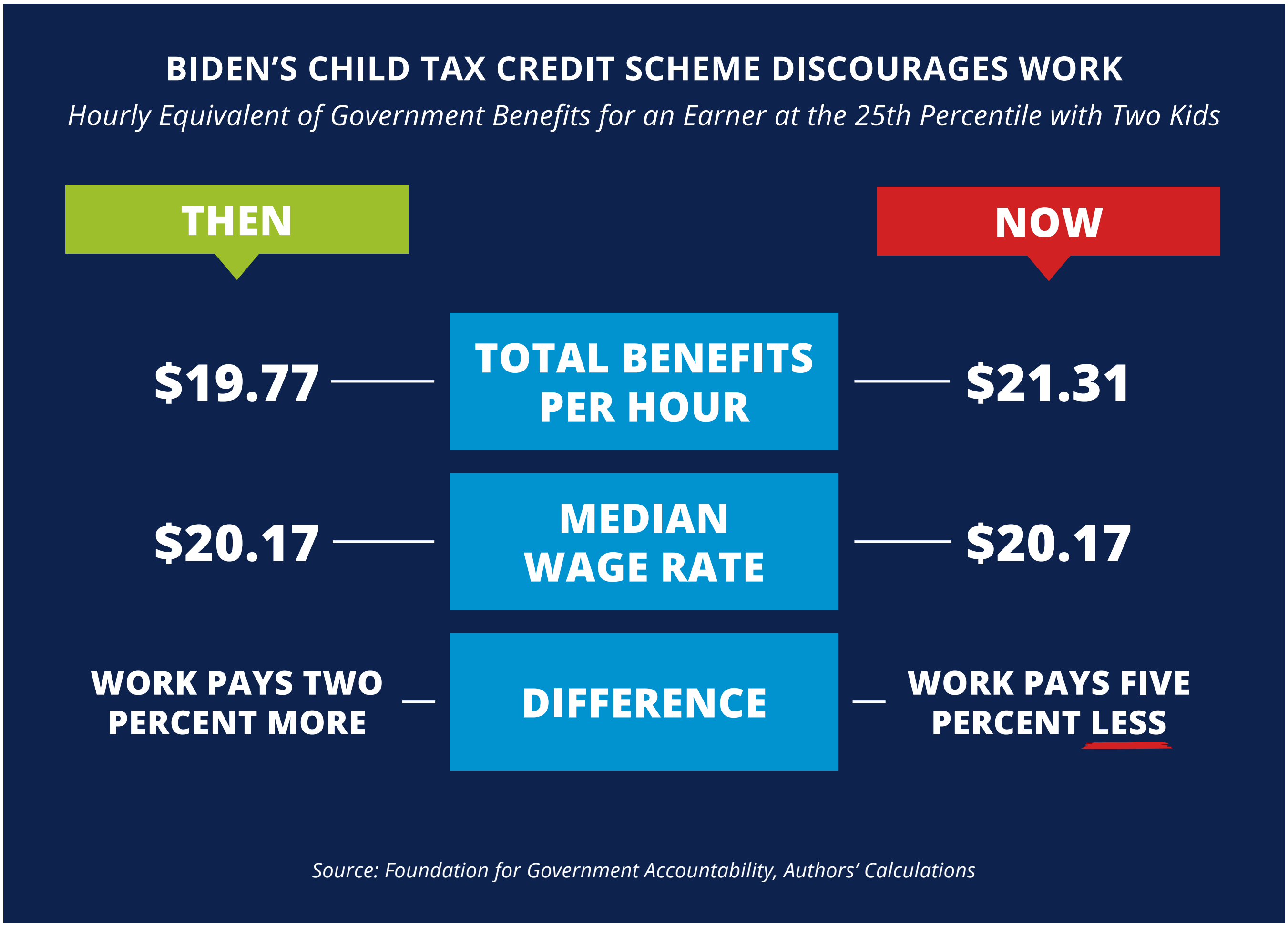
Specifically, when the value of cash benefit programs is combined with the prior Child Tax Credit, it still pays less than the median wage for many Americans.[6] But when these cash benefit programs are coupled with the new Biden Child Tax Credit scheme, it pushes benefits beyond the median wage for countless Americans.

> **“When these cash benefit programs are coupled with the new Biden Child Tax Credit scheme, it pushes benefits beyond the median wage for countless Americans.”**

Imagine a scenario of a single parent with two kids, who previously worked at a relatively low-income job. That parent—called “Dave” for this scenario—finds out he is eligible for food stamps, the Earned Income Tax Credit (EITC), regular unemployment benefits, and the federal $300 weekly unemployment bonus.

But for Dave, it still makes financial sense to look for another job—that is, until the Biden Child Tax Credit scheme enters the picture.

Before the Biden Child Tax Credit scheme, it paid more for Dave to work.[7] But under the new scheme, it pays less for Dave to look for work and more for him to stay home.[8]



This benefit—which is further enticing for Dave because it is distributed in regular, predictable payments—makes the difference between being paid to work and being paid to stay home.

3 THE BIDEN CHILD TAX CREDIT SCHEME TRANSFORMS AN IMPORTANT ANTI-POVERTY TOOL INTO "FUN MONEY" FOR THE MIDDLE CLASS.

Supporters of the Biden Child Tax Credit scheme will eagerly admit that, unlike before—when the Child Tax Credit operated more like an anti-poverty measure—the new tax credits "will go to almost every parent in the nation" outside of the extreme high end of the income spectrum.[9]

What they are really saying is that tax relief for the poor has been turned into monthly payments for the financially secure.

In fact, the top one percent of earners will see a 3.3 percent increase in their average benefit under the Biden Child Tax Credit scheme.[10] Additionally, because of the structure of the new Biden Child Tax Credit scheme, many higher-income households will see a larger percent increase in their payments from the government compared to lower-income families.[11]

Less than half of the value of the Biden Child Tax Credit scheme will go to households in poverty.[12] This is not a poverty-reducing program—it is a dependency-inducing program.

LESS THAN HALF OF THE VALUE OF THE BIDEN CHILD TAX CREDIT SCHEME WILL GO TO HOUSEHOLDS IN POVERTY.

4 THE BIDEN CHILD TAX CREDIT SCHEME SENDS THOUSANDS OF DOLLARS TO PEOPLE WHO DO NOT WORK AT ALL.

Before the Biden Child Tax Credit scheme, individuals were required to earn at least $2,500 per year in order to qualify for the Child Tax Credit. Even then, they were only eligible for a refund of up to $1,400 per dependent if their credit exceeded their tax liability.[13] Put simply, if an individual was not working, they would not be eligible for any credit. And if they only worked the bare minimum, they could not receive the full $2,000 credit per dependent. This policy rewarded working families.

Under the Biden Child Tax Credit scheme, the entire credit is fully refundable and there is no minimum earnings requirement.[14] Now, individuals who do not work—e.g., those who have no earned income—receive the full value of the credit.

Put simply, a program that previously offered working families a break has been transformed into a set of payments that rewards choosing not to work.

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Even worse, refundable tax credits only work when the tax liability is known. Now, the IRS is forced to simply make their best guess of eligibility by using Americans' most recent tax return. While this may not be as large a problem for high-income earners who can shoulder the expense at tax time next year, low-income earners might not be as financially prepared for a sudden tax liability.

5 THE BIDEN CHILD TAX CREDIT SCHEME WILL HURT FAMILIES AT TAX TIME.

The Biden Child Tax Credit scheme will hurt families at tax filing time in 2022, primarily because these checks are being sent out based on government assumptions, not real-time data. When the IRS has to guess at Americans' income, it is bound to be incorrect—and it is everyday Americans who will be on the hook at tax time as they learn they were ineligible for payments the government automatically enrolled them in.

This sets the course for an unavoidable nightmare when millions of lower-income Americans spend the monthly payments, earn more in 2021 than the IRS guessed they would, and then get hit with an unexpected tax bill next year.

LOWER-INCOME AMERICANS WHO SPEND THE MONTHLY PAYMENTS BUT EARN MORE IN 2021 THAN THE IRS GUESSED THEY WOULD, WILL GET HIT WITH AN UNEXPECTED TAX BILL NEXT YEAR.

The Congressional Research Service quietly acknowledges this all-but-certain headache for working families at tax time next year: "In cases where a taxpayer receives more in advance payments than the total 2021 credit they are eligible for, they will generally need to repay any excess credit."[15]

Unfortunately, these clawbacks by the IRS will not just be limited to changes in income. If a family's filing status changes year over year, they can suddenly find themselves on the hook for a big check to the IRS.[16] For example, if a taxpayer's filing status or number of qualifying children changes, it could also result in a clawback.[17]

This all speaks to what should be the final nail in the coffin of the Biden Child Tax Credit scheme—that is, the failed record of past attempts to administer similar tax credits in this manner.

6 PAST TAX SCHEMES OF THIS KIND FAILED MISERABLY.

In the 2000s, individuals were allowed to receive the Earned Income Tax Credit (EITC) through advance payments as part of regular paychecks—much like the Biden Tax Credit.[18] Unfortunately, the program was a bureaucratic nightmare.

Unsurprisingly, the program was riddled with errors: 20 percent of recipients had invalid Social Security numbers, representing nearly $40 million in payments.[19] Additionally, 40 percent of recipients did not file the required tax return, while two-thirds of the remaining participants misreported their credit.[20]

20 PERCENT OF RECIPIENTS HAD INVALID SOCIAL SECURITY NUMBERS, REPRESENTING NEARLY $40 MILLION IN PAYMENTS.

Ultimately, in 2010, the Obama administration announced plans to finally put the failed experiment out of its misery citing the same Government Accountability Office (GAO) report, which also indicated that 80 percent of program recipients failed to comply with program requirements.[21-22]

Unfortunately, history is doomed to repeat itself in 2021 with the advance payments of the Biden Child Tax Credit scheme. And if individuals do not file tax returns next year, this will prevent the ability to fix the errors that are bound to occur by automatically enrolling ineligible individuals. This further underscores why this tax credit experiment should follow the path of its EITC predecessor and be tossed aside.

THE BOTTOM LINE: Congress should end the Biden Child Tax Credit scheme.

Between backwards incentives, IRS clawbacks from low-income earners, and the all-but-certain reality of administrative errors, the Biden Child Tax Credit scheme was a failed experiment before it was even implemented.

While some are discussing making it permanent—**at the cost of $1.6 trillion over the next decade**—the best thing Congress can do is let it expire at the end of 2021.[23] While Congress might currently be unaware of all the perils it will cause, there will be a wave of pain felt by millions of Americans' pocketbooks next tax season as this program causes unexpected tax liability increases.

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