



# Issue Brief: The Child Tax Credit

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## How Does the Child Tax Credit Work?

The Child Tax Credit provides tax-based assistance to families with children. Families can claim up to \$1,000 for each child, reducing the amount they owe in taxes, and under certain circumstances, increasing the amount of their yearly tax refund. The CTC provides families with additional funds that can help them cope with the rising costs of maintaining a household and raising children. Yet due to the way the credit is structured, low-income families are more likely than middle-income families to be denied the full benefits of the credit.

The credit has two components:

1. **Basic Child Tax Credit (Non-Refundable).** The basic CTC provides an offset against tax liability of up to \$1,000 per child under the age of 17. This amount is not adjusted for inflation. This credit is only available to families with tax liabilities, so it provides little or no benefit to lower-income families who owe little to no money in federal income taxes.
2. **Additional Child Tax Credit (Refundable).** Families that don't fully benefit from the non-refundable credit may be eligible for the additional child tax credit, which is refundable. Refundable credits can result in a net payment, or refund, to the taxpayer beyond what he or she actually owes in taxes. A family's additional child tax credit in 2008 is equal to 15 percent of all earnings above \$12,050, up to the maximum \$1,000 credit per child. Thus, families making \$12,050 and under will not receive any benefit under the additional child tax credit.

The Child Tax Credit should therefore be made fully refundable for all low-income children. The amount of the credit should also be adjusted for inflation so that it retains its value over time.

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## The Child Tax Credit in Action: Meet the Smiths

The Smith family has two parents, two children, combined yearly earnings of \$14,050, and a tax liability—the amount that should have been paid in taxes over the course of the year—of \$0 for tax year 2008.

1. **Basic Child Tax Credit (Non-Refundable):** The Smiths qualify for a \$2,000 credit (\$1000/child). But given their limited earnings, they do not owe any money in federal taxes for the year. They will therefore not benefit from the \$2,000 credit for which they qualify. If this tax credit were refundable, the Smiths would collect the \$2,000 from the IRS as a part of their return.
2. **Additional Child Tax Credit (Refundable):** The Smiths can get some added benefit from the refundable additional child tax credit. They make \$2,000 more than the minimum required salary of \$12,050. Fifteen percent of \$2,000 is \$300. Since this component of the credit is refundable, they will receive an additional payment of \$300 from the IRS.

The total benefit to the Smiths is \$300 in the form of an additional cash payment to the family.

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## Questions and Answers

### How do CTC rules exclude, or limit the participation, of low-income families?

Low-income families face certain barriers in trying to collect the additional child tax credit. The value of a family's credit increases as their earnings increase, creating the least benefit for those with the lowest incomes. Children in any family with earnings below \$12,050 are wholly ineligible for the child tax credit in 2008.

Program rules create another barrier under the additional child tax credit because the income floor increases each year according to inflation. Families must make more money each year in order to continue to qualify. Unfortunately, the federal minimum wage is not similarly indexed to inflation, and it took 10 years to secure the most recent increase. The wages of low-income workers making above minimum wage have also stagnated in recent years. The CTC moves further out of reach for those workers who don't receive raises in their income as the minimum income required to receive the additional child tax credit steadily climbs.

### How many low-income children are denied full or partial benefits?

An estimated 10.6 million children in low-income families were ineligible for the CTC in 2007, and an additional 11 million low-income children received less than the full credit amount.

## Which children receive a reduced child tax credit or no credit?

African-American and Hispanic children are the least likely to benefit from the CTC. Nearly 50 percent of African-American children and 46 percent of Hispanic children receive no credit, or only a partial credit, because their families have low or no earnings. Only 18 percent of white children fit within that category.

## What other characteristics describe families that are excluded, or limited, in their CTC participation?

Over half of the children who do not receive any benefits—51.9 percent—are from working families. Minimum wage workers and those with earnings near the poverty line are likely to only qualify for a partial child tax credit. Although many parents are in low wage jobs, yearly earnings may be too low to qualify for benefits when time is spent away from the workforce due to reasons such as involvement in temporary or itinerant employment, participation in education or job training, pregnancy, or parental or child illness.

## How do high- and middle-income families fare under the CTC as compared to low-income families?

The CTC begins to phase out for two-parent families making more than \$110,000 per year, or \$75,000 for single parents and \$55,000 for married couples filing separate returns. Unlike the income requirements for low-income families, these numbers are not indexed for inflation.

According to the Tax Policy Center, 95 percent of CTC benefits go to households with incomes between \$20,000 and \$200,000. The beneficiaries that get the highest monetary value out of the credit are those with incomes between \$75,000 and \$100,000.

## Why should the CTC be available to families with little or no income tax liability?

The CTC is the principal federal strategy for providing income assistance to families with children, helping them to afford the costs of child rearing. Low-income children should not be excluded from benefits. Their families are equally, if not more so, in need of such assistance. In addition to having less money with which to raise their children, they often pay a higher cost for being poor. The same consumer products and financial services purchased by middle- and high-income families tend to have a higher price tag for low-income families.

## How would making the CTC fully refundable affect poverty?

The Urban Institute found that making the CTC fully refundable would reduce poverty by 9.2 percent and deep poverty by 11.5 percent. This equates to 3.3 million people, including 2.1 million children. Their findings further indicated that, combined with increasing the minimum wage, expanding the Earned Income Tax Credit, and increasing child care assistance, making the CTC fully refundable would reduce poverty by 26 percent.

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## Additional Resources

[Background Basics: How Does the Child Tax Credit Work?](#)

[The Child Tax Credit in Action: Meet the Smiths](#)

[Q & A on the Child Tax Credit](#)

The Center on Budget and Policy Priorities ([www.cbpp.org](http://www.cbpp.org))

The Coalition on Human Needs ([www.chn.org](http://www.chn.org))

The Tax Policy Center ([www.taxpolicycenter.org](http://www.taxpolicycenter.org))