Expanding the Child Tax Credit

In 2017, Senator Lee and Senator Rubio pushed to increase the Child Tax Credit (CTC) in the Tax Cuts and Jobs Act. As a result of their effort, the CTC was doubled to $2,000 and its refundability was increased by more than 25 percent. Still, the final product fell short in several respects:

(1) The credit only offsets a fraction of the parent penalty imposed on working families,
(2) Refundability does not begin until after the first $2,500 of earnings, and
(3) Only the first $1,400 of the credit is refundable against payroll tax liability.

Accordingly, Senators Lee and Rubio have continued to call on Congress to further expand the CTC and address these lingering issues. They have been encouraged by the recent efforts of others to increase the CTC. Many elements of such proposals would make progress in addressing the parent penalty in current U.S. tax code and are a welcome contribution to the conversation.

Senators Lee and Rubio hope to expand the discussion by offering their own proposal, one which would offer more tax relief for working families, cost tens of billions less than the Biden plan, and would neither turn the CTC into a new entitlement program nor attempt to influence parents' child-care decisions.

Bill Specifics

- Would fix the refundability of the CTC so that working parents are able to receive the full credit, starting with their first dollar earned, up to their total federal tax liability (income and payroll).
    - Refundability to include payroll liability is a natural tax break for working families that contribute to the future of Social Security and Medicare by raising the country's future workforce. This is different from a welfare program in that a family would be able to keep more of their own earnings to offset the costs of childrearing.
- Would repurpose the Child and Dependent Care Tax Credit and related provisions to offset an increase to the CTC for young children, thereby eliminating the stay-at-home parent penalty.
    - Through the Child and Dependent Care Tax Credit and other flexible spending account provisions, dual-earner families who contract for professional child care are provided additional tax relief denied to families who have a parent that stays at home or uses less formalized child care.
- Would expand the CTC to $3,500 with an $1,000 enhancement for those with children aged five and under (total young-child credit of $4,500).
    - By turning the CDCTC into an enhanced CTC for young children, families would be equipped with flexibility to tackle the larger health-care and child-care expenses that often come with children at this stage.

Addendum I:
The Parent Penalty

The parent penalty refers to the additional financial burden parents incur due to our tax and entitlement structures. Through the requisite expenses to raise a child and payroll taxes, parents contribute to Social Security and Medicare not once but twice.

According to the most recent estimates from the United States Department of Agriculture, the average family will spend $233,610 to raise a child from birth to age 18 (between $12,350 and $13,900 annually).[1] A family with two children making the median household income ($68,703 in 2019) will pay $189,216 over 18 years in payroll taxes ($10,512 annually) in addition to the $467,220 they pay to raise the next generation of workers who will also pay into Social Security and Medicare.

Compared to a couple making the same amount but with no children (and thus no childraising expenses), the family with two children is paying nearly four times as much over 18 years—payments which will contribute directly or indirectly to the funding of Social Security and Medicare benefits for not only themselves but also for those without any children.

Addendum II:
The Stay-At-Home Parent and
Alternative Care Arrangement Penalty

The Child and Dependent Care Tax Credit (CDCTC) and related childcare flexible spending accounts (FSA) help subsidize the costs of formal child care for working parents. The CDCTC alone can provide up to $2,100 a year per family.[2] Families that elect other forms of child care, including having a parent stay at home or arranging for a family friend or relative to babysit without compensation, are ineligible for the CDCTC and childcare FSA benefits and are therefore disadvantaged. This is the stay-at-home parent penalty, and the Biden Administration's proposal would make it nearly seven times worse.[3]

Government and the tax code are utterly unequipped to determine the best child-care course of action for children or families. Accordingly, the tax code should not favor one type of child care over others, effectively penalizing families with a parent who chooses to stay at home or utilize informal child care.

[1] https://www.usda.gov/media/press-releases/2017/01/09/families-projected-spend-average-233610-raising-child-born-2015
[2] While the maximum annual CDCTC benefit is $2,100 ($175 monthly), the credit gradually phases down to $1,200 ($100 monthly) for families with more than $15,000 in adjusted gross income. https://fas.org/sgp/crs/misc/R44993.pdf
[3] The median American household's total CDCTC benefit would go from $1,200 to $8,000 under the Biden plan. https://www.whitehouse.gov/briefing-room/legislation/2021/01/20/president-biden-announces-american-rescue-plan/