

TAX BREAKS

Warning: You May Have to Pay Back Your Monthly Child Tax Credit Payments

Unlike stimulus checks, you might have to repay your monthly child tax credit payments if you get too much money from the IRS.



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The IRS is now making monthly child tax credit payments to eligible families. Depending on the age of your child, those payments can be as much as \$300-per-kid each month from July to December. That's an extra \$1,800 per child in your pocket if you get the full amount for six months. But what if the IRS sends you too much money – do you have to pay it back? Maybe.

When the IRS was doling out stimulus check money, they occasionally overpaid someone. But there was nothing in the law requiring repayment of a stimulus check. So, if you got too much, you generally were allowed to keep it.

But that's not the case with the monthly child tax credit payments. The law authorizing these payments specifically says that any excess amounts must be paid back when you file your 2021 tax return if your income is above a certain amount. There are exceptions to this rule for middle- and lower-income families, but they're limited. Plus, the way the monthly payments are calculated, overpayments could be fairly common. So, this could be a big issue for a lot of families.

Changes to the Child Tax Credit for 2021

Before getting into how you might end up with an overpayment and the details of the payback rules, it's probably a good idea to go over some of the changes to the child tax credit that apply for the 2021 tax year (and, so far, only for 2021). Last year, the maximum child tax credit was \$2,000 per child 16 years old or younger. It was also phased-out if your income exceeded \$400,000 for married couples filing a joint return or \$200,000 for single and head-of-household filers. For some lower-income taxpayers, the credit was partially "refundable" (up to \$1,400 per qualifying child) if they had earned income of at least \$2,500 (i.e., you got a refund check for the refundable amount if the credit was more than the tax you owed).

The American Rescue Plan, which was enacted in March, made some major changes to the child tax credit for the 2021 tax year. For one thing, the credit amount was raised from \$2,000 to \$3,000 for children 6 to 17 years old and to \$3,600 for kids 5 years old and younger. The \$2,500 earned income requirement was also dropped, and the credit was made fully refundable (which means refund checks triggered by this year's credit can be greater than \$1,400).

There are also two phase-out schemes in play for families with higher incomes in 2021. The first one can't reduce the credit amount below \$2,000 per child. It kicks in if your modified adjusted gross income (AGI) is above \$75,000 (single filers), \$112,500 (head-of-household filers), or \$150,000 (joint filers). The second phase-out is the same \$200,000/\$400,000 one that applied before 2021.

Finally, the American Rescue Plan requires the IRS to pay half of your total credit amount in advance through monthly payments issued this year from July to December (you can opt-out if you want). In most cases, the IRS will base the amount of these payments on information it pulls from your 2020 tax return. Next year, you'll claim the remaining half of the credit on your 2021 tax return. In practice, this will be done by subtracting every dollar you received from July to December from the total credit you're entitled to claim and then reporting the leftover amount, if any, as a child tax credit on your 2021 return. (Use our 2021 Child Tax Credit Calculator to see how much your monthly payments will be and what should be leftover to claim as a credit on your 2021 tax return.)

How Child Tax Credit Overpayments Can Occur

You may be wondering why the IRS would send you too much money in the first place. If the goal is simply to give you a 50% advance of your total child tax credit over a six-month period, it doesn't seem like that would be too difficult. It's basic math – right?

Well, yes, the math itself is easy...but things change, which can make it difficult to find the right numbers to plug into the computers. For instance, what if your income increases in 2021 to a point where your child tax credit is now partially or completely phased out. The IRS is going to look at your 2020 tax return to calculate the amount of your monthly payment. If your 2020 income was below the credit's phase-out thresholds, the IRS is probably going to send you the maximum amount each month. However, because of your higher 2021 income, your 2021 child tax credit is going to be lower than expected...which could create an overpayment.

Since the child tax credit phase-out thresholds are tied to your filing status, a similar situation can arise from a change to your family situation in 2021 (e.g., a divorce). For example, imagine that the IRS bases your monthly payments on your 2020 joint return and your 2021 income is lower than the credit phase-out threshold for joint filers. You then use a different filing status on your 2021 return with a lower credit phase-out threshold (e.g., single or head-of-household) that results in a reduced child tax credit amount. That can also generate an overpayment.

If you claim the child tax credit for fewer children in 2021 than you did in 2020, that can result in an overpayment, too. This can happen, for instance, if you're divorced and you claimed your child as a dependent on your 2020 tax return, but your ex-spouse claims the child as a dependent for 2021 taxes (a common arrangement). In that case, the IRS is going to send you monthly payments for the child. However, since you won't qualify for the child tax credit on your 2021 return (your ex will), all the money you received from July to December will be an overpayment.

And here's one more example...your main home must be in the U.S. for more than half of 2021 to qualify for monthly child tax credit payments. If you satisfied that requirement in 2020, but not in 2021, the IRS could end up sending you monthly payments that you're not supposed to get. That can result in an overpayment as well.

Payback Requirements for the 2021 Child Tax Credit

Now let's talk about what happens if you end up with a child tax credit overpayment. Depending on your income, you **might** have to pay some or all of it back as an addition to the tax you owe when you file your 2021 return next year.

Lower-income people get a good deal. If your modified AGI for 2021 doesn't exceed \$40,000 (single filers), \$50,000 (head-of-household filers), or \$60,000 (joint filers), and your principal residence was in the U.S. for more than half of 2021, you won't have to repay any overpayment amount. That's a win for you!

On the other hand, parents with higher incomes don't get any breaks at all. If your modified AGI for the 2021 tax year is at least \$80,000 (single filers), \$100,000 (head-of-household filers), or \$120,000 (joint filers), you have to pay back your entire overpayment. Ouch!

It's a little more complicated for people in the middle. All or part of your overpayment might be forgiven if your modified AGI for 2021 is between \$40,000 and \$80,000 (single filers), \$50,000 and \$100,000 (head-of-household filers), or \$60,000 and \$120,000 (joint filers). To determine how much of your overpayment is wiped out (if any), you first need to calculate what the IRS calls your "repayment protection amount." This is equal to \$2,000 multiplied by:

- The number of children the IRS used to calculate your monthly child tax credit payments, minus
- The number of children used to calculate the total credit amount on your 2021 tax return.

If there's no difference between the number of children used to calculate the two amounts, then there's no overpayment reduction, and the full amount must be repaid. If you have a positive repayment protection amount, it's then gradually phased-out as your modified AGI increases within the income range above. The phase-out rate is based on how much your modified AGI exceeds the lower limit of the applicable income range. Once your final repayment protection amount is calculated, it's subtracted from your overpayment to determine how much you need to repay (but your overpayment can't be reduced below zero).

Here's an example of how this works: Joe, who is single, claimed a child tax credit for two children on his 2020 tax return (the children are 2 and 4 years old at the end of 2021). As a result, the IRS sent him \$3,600 in monthly payments in 2021. However, Joe can't claim the child tax credit on his 2021 return because his ex-wife is claiming the children as dependents on her return. Since his 2021 child tax credit is \$0, the entire \$3,600 he received from the IRS is an overpayment. Joe's initial repayment protection amount is \$4,000 (i.e., \$2,000 for each child). If Joe files a 2021 return with a modified AGI of \$60,000, his modified AGI exceeds the lower limit of the applicable income range – \$40,000 – by 50% ($\$60,000 - \$40,000 / \$80,000 - \$40,000 = 0.5$). As a result, Joe's \$4,000 repayment protection amount is reduced by 50% to \$2,000. Therefore, Joe only has to repay \$1,600 of his \$3,600 overpayment ($\$3,600 - \$2,000 = \$1,600$).

[Note: You may also have to pay a portion of your overpayment if your modified AGI is less than or equal to \$40,000 (single filers), \$50,000 (head-of-household filers), or \$60,000 (joint filers) and you lived outside the U.S. for at least half of 2021.]

How to Prevent Child Tax Credit Overpayments

If you think an overpayment is in your future, there are two things you can do to minimize or eliminate any potential repayment obligation. First, you can opt-out of the monthly payments. If you're no longer receiving monthly payments, then you might be able to avoid an overpayment altogether (just make sure you meet the deadline for opting out before the next scheduled payment). If you've already received enough money from the IRS to create an overpayment, opting out can at least prevent the overpayment from growing larger.

To opt-out, go to the Child Tax Credit Update Portal on the [IRS's website](#). You'll need either an existing IRS account or an [ID.me](#) account to access the online tool. Although you can't do it now, later this summer you'll be able to restart monthly payments through the portal if you previously opted out.

You can also control a potential overpayment by updating any outdated information concerning your income, filing status, or qualifying children that the IRS pulled from your 2020 return or collected from some other source. Once the IRS gets the new information, it can adjust (i.e., lower) your remaining monthly payments to account for the change. This could also prevent or reduce an overpayment.

You'll have to use the Child Tax Credit Update Portal to report any updates. However, this functionality is not available yet. Again, it should be ready later this summer.

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