To Reach Every Child, the Child Tax Credit Eligibility Requirements Must Be Changed - June 2021

The American Rescue Plan Act (ARPA), signed into law in March, includes a significant, one-year expansion to the Child Tax Credit (CTC), which will help increase children's access to a regular and meaningful cash benefit program beginning in July. Millions of newly eligible children and their families will benefit from this major expansion and successful implementation is critical to effectively build income security, reduce child poverty, advance racial equity, and provide the baseline for a guaranteed income for all children.

While approximately 23 million children will be newly eligible for the full value of the CTC because of this expansion, many children will still be left out due to arcane tax rules. Specifically, more than 300,000 children are excluded from the CTC because of strict eligibility requirements known as the “child claiming” rules that deny benefits to children whose primary caregivers are more distant relatives or family friends and to children who do not live with a single caregiver for six months out of the year. Together, these rules deny CTC benefits to many children who move frequently between households or have a relationship with their caregiver different than those enumerated in the tax code. These children are often immigrants, involved in the child welfare system, experiencing homelessness, or involved with the juvenile justice system.

To ensure that no child is excluded from the CTC because of their family structure, frequency of moving, or their involvement in other systems, Congress must make critical changes to the definition of “qualifying child” for the purpose of the CTC. To expand eligibility, the CTC should be accessible to all children regardless of their relationship to their caregiver and the benefit should continue to support children and their families as their living arrangements change.

What Are the “Child-Claiming” Rules that Restrict Access to the CTC?

The expanded CTC will be available to taxpayers with children under age 18 with Social Security Numbers (SSN) even if they have little or no income, as long as those taxpayers satisfy a few additional tests known as the “child-claiming rules.” Most prominent among those rules are:

- **The Relationship Test:** A taxpayer may claim the credit only if they are the child's parent, grandparent, sibling, aunt or uncle (or a similarly close step-relative or relative by marriage).

- **The Residency Test:** A taxpayer may claim the credit only if they reside with the child for at least half of the year (six months) in which the credit is claimed.

Who Do These Tests Leave Out?

These rules deny benefits to hundreds of thousands of children simply because they do not satisfy the existing child-claiming rules. For instance, the Relationship Test specifically disqualifies children whose primary caregivers are more distant relatives, such as cousins, or fictive kin,
such as close family friends or chosen family. In total, about 330,000 children, disproportionately Hispanic children, are excluded because of the relationship test alone.

The Residency Test denies benefits to children who may not spend at least six months in any single household and thereby disqualifies certain children who move between the homes of different family members or caregivers throughout the year, whose caregivers have split custody arrangements, who are unhoused, or who spend a portion of the year in out-of-home placements in the child welfare or juvenile justice systems. It is difficult to know exactly how many children are excluded from the CTC based on the Residency Test alone, though every year millions of children experience housing instability, homelessness, or placement in the child welfare or juvenile justice systems.

How Can We Fix this Problem?

Ensuring every child is eligible for the CTC requires overhauling the child-claiming rules and determining eligibility on a monthly basis. Congress must ensure that all children benefit from the expanded CTC and are eligible regardless of their family structure or how often they move.

To ensure every child is eligible for the CTC and that the benefit follows the child throughout the year, we recommend the following changes:

- **Replacing the existing child-claiming rules with a single “Primary Caregiver” Test:** Under this new test, all children can be claimed by their caregiver, regardless of the caregiver’s legal or formal relationship to the child. A primary caregiver is someone who lives with a child during a given month and is responsible for things like supervising the child’s daily activities and needs, making sure the child’s medical needs are met, and arranging for child care when necessary.

- **Monthly eligibility:** Eligibility would be determined monthly, with a requirement that the primary caregiver reside with the child “for a significant part of the month” in which they receive the CTC on behalf of the child—i.e. 50 percent or more of that month (cases in which two caregivers equally divide responsibilities are discussed below). After the initial determination of eligibility, the benefit will continue going to the primary caregiver on file each month by default. For cases in which a child stays with the same family consistently, the primary caregiver would have to file their taxes or fill out a simplified filing tool no more than once a year stating that a child “still lives with me” for purposes of claiming the CTC. When a child moves in with a new primary caregiver, the caregiver would establish eligibility by filling out a simple form on an online portal or checking a box on their tax return to claim the benefit starting that month.

- **Competing claims:** In cases where two caregivers equally divide caregiving responsibility, they should be able to share the “primary caregiver” distinction and split the benefit evenly, or agree to assign the benefit to one of them. If two or more caregivers claim the benefit on behalf of a child and dispute who is the primary caregiver, the IRS should adjudicate the dispute in a timely manner.

- **Children on their own:** In cases where a youth has no relationship to an adult caregiver, the youth should be able to claim the credit on their own behalf.
These modified rules would reach most children currently excluded, but special exceptions must also be created to ensure the unique needs of certain populations are met, such as:

- **Youth who are unhoused:** Youth aged 15 and older who experience homelessness on their own, unsupported by and not living with a parent, should claim the CTC on their own behalf. Too often, youth who are unhoused are already living in poverty and experiencing severe economic distress and need additional support—the CTC can provide this much needed support. In order for a youth to claim it on their own, community service providers and McKinney-Vento school liaisons could help this population sign up. Additionally, the IRS should help develop a process for these vulnerable children and should help mitigate the risk of competing claims through a “hierarchy of claims.” Under the hierarchy, parents could still claim the CTC, but if their child claimed it on their own behalf as an unaccompanied youth, the child’s claim would supersede the parent’s claim.

- **Children in the child welfare system:** For children in out-of-home placements in the child welfare system, the CTC should stay with birth parents for at least 12 months, or until the Termination of Parental Rights (TPR), whichever comes earlier. Additionally, the Secretary of Health and Human Services should be directed to work with the Secretary of the Treasury and the Commissioner of Internal Revenue to develop guidance around extending eligibility to birth parent(s) with children in foster care beyond 12 months in circumstances in which the parent(s) are continuing to work toward reunification. If the birth parent(s) is not eligible to receive the payment, the CTC would be held in the child’s name in an account to grow tax free and to be claimed by the child upon their exit from care. The account could be similar to an Individual Development Account (IDA), but without limitations placed on eligible uses. Any cash in the account would not count as assets for the purposes of determining eligibility for public benefits or other government programs, including Title IV-E eligibility.

- **Youth in the juvenile justice system:** Families with a youth living outside of the home because they are detained, placed, or incarcerated should be able to claim the CTC for at least six months. After that period, the CTC should be held in the youth’s name in an account to grow tax free and to be claimed by the youth upon their release. The account could be similar to an Individual Development Account (IDA), but without limitations placed on eligible uses. Any cash in the account would not count as assets for the purposes of determining eligibility for public benefits or other government programs, including Title IV-E eligibility.

It is time to allow the CTC to respond to the reality of families’ lives. These child-claiming rules and limitations around which children can access the CTC have been around for decades, disproportionately hurt children of color and immigrants, and must be changed. The pandemic has clearly highlighted the pre-existing economic instability and inadequate federal support felt by so many families across the country. Now, a permanent child allowance, which will provide that stability, is on the horizon in Congress. It is time for Congress to rewrite the child-claiming rules to ensure the CTC follows each child, no matter their household composition, family structure, or where they live.