
Advance Child Tax Credit and Third Round Stimulus Payments to Be Reconciled on Your 2021 Return

Early in 2021 Congress passed the American Rescue Plan which included a provision that increased the child tax credit amount and upped the age limit of eligible children. Normally, the credit was \$2,000 per eligible child under age 17. For the 2021 tax year the American Rescue Plan increased the credit to \$3,000 for each child under age 18 and to \$3,600 for children under age 6 at the end of the year.

Even though the benefit of a tax credit traditionally isn't available until after the tax return for the year has been filed, for 2021 the new tax law included a provision to get the credit benefit into the hands of taxpayers as quickly as possible and charged the Secretary of the Treasury with establishing an advance payment plan. Under this mandate, those qualifying for the credit would receive monthly payments starting in July equal to 1/12 of the amount the IRS estimated the taxpayer would be entitled to by using the information on the 2020 return. If the 2020 return had not been filed or processed yet by the IRS, the 2019 information was to be used.

However, since the IRS only estimated the amount of the advance payments, some taxpayers may have received too much and others not enough. Thus, the payments received must be reconciled on the 2021 tax return with the amount that each taxpayer is actually entitled to. Those who received too much may be required to repay some portion of the advance credit while some may be entitled to an additional amount.

To provide taxpayers with the information needed to reconcile the payments, the IRS started sending out Letter 6419, an end-of-year statement that outlines the payments received as well as the number of qualifying children used by the IRS to determine the advance payments. For those who filed jointly on their prior year return, each spouse will receive a Letter 6419 showing the advance amount received.

Do not discard the letter(s) from the IRS as they will be helpful in properly filing 2021 returns.

Having received the advance credit payment, taxpayers will find their refunds will be substantially less than they may have expected, or they might even end up owing money on their tax return unless their AGI is low enough to qualify for the safe harbor repayment protection for lower-income taxpayers, in which case the excess advance repayment is eliminated or reduced.

Example: *If a taxpayer received advance child tax credit payments for two children based on the 2020 return, and the taxpayer doesn't claim both children as dependents in 2021, the taxpayer would need to repay the excess on their return, unless they are protected by the safe harbor provision.*

It is also possible that one taxpayer could have received the advance child tax credit payments based on their 2020 return and not have to make a repayment under the safe harbor rule, while another taxpayer, who can legitimately claim the child, can get the credit on their 2021 tax return. This is most likely to happen when the parents are divorced. So, there's the potential for the child tax credit to be received by both parents.

Third Round Economic Stimulus Payments - The IRS will begin issuing Letter 6475, regarding the third Economic Impact Payment, to EIP recipients in late January. This letter will help EIP recipients determine if they are entitled to and should claim the Recovery Rebate Credit on their tax year 2021 tax returns filed in 2022.

Letter 6475 only applies to the third round of Economic Impact Payments that were issued starting in March 2021 and continued through December 2021. The third round of EIPs, including the "plus-up" payments, were advance payments of the 2021 Recovery Rebate Credit that would be claimed on a 2021 tax return. Plus-up payments were additional payments the IRS sent to people who received a third EIP based on a 2019 tax return or information received from the Social Security Administration, Railroad Retirement Board or Dept. of Veterans Affairs; or to people who may be eligible for a larger amount based on their 2020 tax return.

Most eligible people already received the payments. However, those who are missing stimulus payments should review the information to determine their eligibility and whether they need to claim a Recovery Rebate Credit for tax year 2020 or 2021.

Like the advance CTC letter, the EIP letter includes important information that can help tax preparers quickly and accurately reconcile the Recovery Rebate Credit when preparing 2021 tax returns.

Please contact this office if you have questions regarding the Child Tax Credit or the Recovery Rebate Credit and the advance payments of either that you received.

Another Rough Tax Season for IRS and Taxpayers?

This could be another rough tax season for the IRS and taxpayers. Although this year's filing season opened January 24, 2022 (i.e., it is the first day the IRS will accept and start processing 2021 returns), the Service still has a backlog of prior year returns to process and is plagued by staff shortages due to the pandemic and reduced funding in the last few years. Even though the majority of 2020 returns were filed electronically, many of those returns still required manual review, resulting in significant delays in IRS issuing refunds. This was the case with millions of 2020 returns of taxpayers who received unemployment compensation and had filed before Congress passed a law that retroactively exempted up to \$10,200 of 2020 unemployment income per filer (that provision has not been extended to 2021). Human review was also required for a significant number of returns on which the Recovery Rebate Credit had to be reconciled with the Economic Impact Payments #1 and #2.

Similar issues are likely to affect 2021 returns, especially those where taxpayers received Advance Child Tax Credit (ACTC) payments and/or Economic Impact Payment #3, both of which must be reconciled on the 2021 return. Thus, to avoid return processing delays it is important to include the correct amounts received when doing the reconciliation. In January the IRS began issuing Letters 6419 (for the ACTC) and 6475 (for EIP #3) to taxpayers; these letters provide the information needed for making the reconciliation calculations. Be sure you provide these letters to your tax return preparer. Having an accurate tax return can avoid processing delays, refund delays and later IRS notices.

Despite reduced staffing and the continuing pandemic, the IRS projects that for this tax season they'll process electronically filed returns and pay refunds that are designated to be direct deposited in the taxpayer's bank account within 21 days of receiving the return. While this turnaround time can't be guaranteed, the earlier you file, the better the chance that you'll see your refund within that time frame. If the IRS systems detect a possible error, missing information, or there is suspected identity theft or fraud, the IRS may need to correspond with the taxpayer, requiring special handling by an IRS employee. In that case, it may take the IRS

more than the normal 21 days to issue any related refund. Sometimes the IRS can correct the return without corresponding, and the IRS will then send an explanation to the taxpayer.

To stop the filing of fraudulent returns, the IRS is prohibited by law from issuing a refund from a return where the Earned Income Tax Credit or Additional Child Tax Credit is claimed until after mid-February. However, that doesn't prevent taxpayers from filing their returns before then.

Taxpayers generally will not need to wait for their 2020 return to be fully processed to file their 2021 tax returns and can file when they are ready. So, if you filed your 2020 return, but the IRS has still not processed it, don't let that stop you from preparing and filing your 2021 return.

In addition to return processing woes, the IRS has had customer service problems, specifically the lack of enough IRS representatives to answer the phone in response to taxpayers' questions. Last tax season, because of Covid-19-related tax changes and staffing challenges, more than 145 million calls were received by the IRS phone system from January 1 – May 17, more than four times the number of calls in an average year. Alas, the Service was able to answer only about 10% of those calls, and callers who were lucky enough to have their calls answered generally had extremely long wait times before actually being able to speak with an IRS employee.

The IRS encourages taxpayers to go to the IRS.gov website to search for answers to their tax questions instead of calling the Service, but that often isn't an adequate substitute for talking personally to a knowledgeable individual. Those who have their returns prepared by a tax pro have the benefit of being able to contact their tax professional with tax questions instead of being frustrated trying to reach or deal with the IRS. Given how understaffed the IRS is, it is more important than ever for taxpayers to have their returns professionally prepared and e-filed when possible.

If you are an existing client and have questions, please give this office a call. If you have been trying to do your own tax return and would like professional preparation, we are here to assist you.

Thank you for selecting our firm for your tax and accounting needs. We appreciate the confidence you have shown in us, and we remain ready to assist you at any time.

Scott Jensen
Kramer & Jensen, LLC

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