Jain Family Institute

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# Correcting the Record on Child Tax Credit Compliance Concerns

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# Contents

1. Summary ↗

2. Why Attention to Improper CTC Payments Is Misplaced ↗

3. Many Solutions to Improper Refundable Credit Claims Are Misguided ↗

4. Conclusion ↗

5. Appendix ↗

# Summary

- IRS data show that incorrect refundable CTC claims make up less than one percent of total tax noncompliance.
- The nonrefundable part of the CTC claimed by middle- and high-income families has a higher improper payment rate than the low-income, refundable portion.
- There is strong evidence that most incorrect CTC payments are benign errors—the bulk of incorrect claims come from close family members or others living with the child, not malicious scammers.
- Many proposed solutions to reform the integrity of the CTC would limit access to the credit. For instance, requiring non-parents to prove they have formal custody of the child they claim would effectively exclude over thirty percent of children not being raised by their parents who do not have formal custody arrangements.

According to recent reporting, some Republicans are concerned about fraudulent claims involving the refundable portion of the Child Tax Credit (CTC)—the part that allows low-earning families to benefit from the credit. For some, the potential for fraud is one reason among many to avoid expanding benefits to low-income families. However, concerns about tax credits going to the wrong people have a long, bipartisan history, and fraud concerns may be a barrier to attracting broad support for expanding the refundable part of the CTC.

Integrity concerns have also led some Republicans to emphasize the need to reform the CTC—as Senator John Cornyn (R-Texas) put it, "we need to eliminate the fraud." An early Ways and Means Committee draft restricts access to the credit for children of undocumented immigrants—a change partly justified as a pro-integrity measure. Think tanks like the Niskanen Center and Bipartisan Policy Center have proposed additional CTC integrity reforms for the 2025 tax debate.

Concerns about fraud in the refundable portion of the CTC are not supported by the evidence. While critics often emphasize how audit practices disproportionately burden low-income families, the core problem is that the fraud concerns themselves are statistically unfounded. Incorrect refundable CTC claims comprise less than one percent of overall tax noncompliance, and the noncompliance rate for the refundable CTC is lower than the rest of the individual income tax code. In fact—within the CTC itself, IRS data show that the refundable part of the credit has a lower rate of incorrect claims than the nonrefundable part that goes to higher-income families.

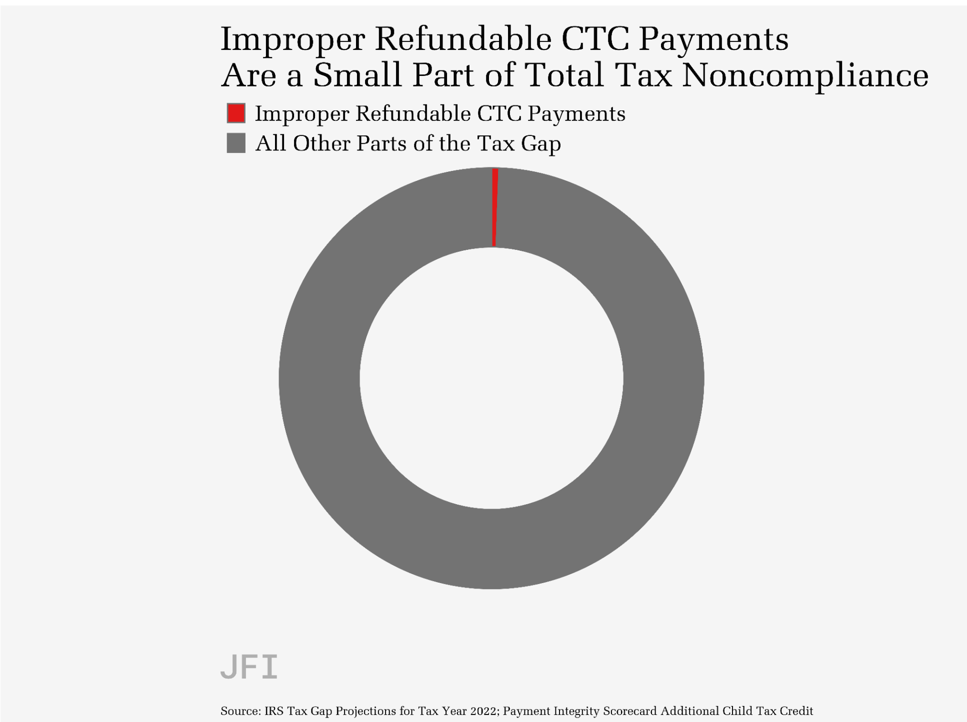
Most “fraud” when claiming children for refundable tax credits like the CTC is benign. Rather than having malicious scammers steal children’s Social Security numbers and claim tax refunds, research has found most incorrect claims come from a close relative or someone helping raise the child who is technically not eligible to claim the credit. These technically improper claims still go to low-income families.

Finally, many proposed solutions aimed at reducing incorrect CTC claims come with an unacknowledged tradeoff of significantly limiting access to the credit by rightful claimants. Designing restrictive policies to address a minor and generally benign part of tax noncompliance is misguided—and especially counterproductive when those policies disqualify previously eligible households. Evidence that these reforms would meaningfully improve compliance is limited, and some proposals may paradoxically reduce access while increasing the likelihood of improper claims.

# Why Attention to Improper CTC Payments Is Misplaced

### Improper refundable CTC payments are a minuscule part of tax noncompliance

The IRS refers to incorrectly issued refundable CTC payments as "improper" payments. These account for less than one percent of total tax noncompliance.[2] If newly implemented reforms caused everyone to claim the refundable CTC correctly, it would have virtually no impact on the overall rate of tax compliance.




[2] The most recent estimate for the total amount of improper CTC payments is $3.4 billion, while the estimated total tax gap (after accounting for enforcement) was $606 billion: Internal Revenue Service. *Federal Tax Compliance Research: Tax Gap Projections for Tax Year 2022*. Publication 5869. Washington, DC: Department of the Treasury, October 2023. https://www.irs.gov/pub/irs-pdf/p5869.pdf; US Department of the Treasury. *Payment Integrity Scorecard: Internal Revenue Service—Additional Child Tax Credit*. Q1 2025 Reporting Period. https://www.cfo.gov/wp-content/uploads/scorecards/FY25-Q1/Internal%20Revenue%20Service%20-%20Additional%20Child%20Tax%20Credit.pdf

A focus on refundable CTC integrity could still be justifiable if it suffered an especially high rate of noncompliance relative to other tax provisions. However, the opposite is true. The refundable CTC actually has a higher compliance rate (89 percent) than the overall individual income tax code (83 percent).[3]

Finally, while Republican concerns about fraud focus on the refundable portion of the CTC (claimed by low-income parents), the nonrefundable portion (claimed by middle- and high-income families) is also prone to improper claims.[4] Poorly targeted bureaucratic requirements cause the refundable portion of the credit to get disproportionate attention, an issue discussed in detail in the appendix of this report. The improper payment rate for the nonrefundable part of the credit is not even published. However, the IRS publishes enough data to make it possible to calculate that the nonrefundable portion of the CTC (the part of the credit claimed by middle- and high-income parents) has a higher rate of noncompliance than the refundable portion claimed by low-income parents. For every dollar spent on the nonrefundable CTC, $0.18 are "improper payments" while for every dollar spent on the refundable CTC, $0.11 are "improper payments."[5] These figures imply that a future CTC expansion going disproportionately to the higher-income portion of the credit would likely increase the credit's overall improper payment rate. No serious effort to improve tax compliance would start by scrutinizing refundable CTC payments.

### Improper payment estimates are methodologically flawed and ignore incomplete take-up, overestimating revenue loss from imperfect compliance

Improper payment rates have several additional problems. For one, the reported methodology improperly conflates errors in the refundable and nonrefundable portions of the credit. I estimate that this inflates the calculated error rate by over 50 percent (details of the calculation are provided in the appendix).

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[3] Internal Revenue Service. Federal Tax Compliance Research: Tax Gap Projections for Tax Year 2022. Publication 5869. Washington, DC: Department of the Treasury, October 2023. https://www.irs.gov/pub/irs-pdf/p5869.pdf; US Department of the Treasury. Payment Integrity Scorecard: Internal Revenue Service—Additional Child Tax Credit. Q1 2025 Reporting Period. https://www.cfo.gov/wp-content/uploads/scorecards/FY25-Q1/Internal%20Revenue%20Service%20-%20Additional%20Child%20Tax%20Credit.pdf

[4] Faler, Brian. "Republicans Look to Blunt Dems' Advantage on Family Tax Credit." *Politico*, April 5, 2025. https://www.politico.com/news/2025/04/05/republicans-family-tax-credit-00266676

[5] Calculations detailed in the appendix.

Additionally, improper payment rates do not account for eligible people who did not claim the credit.[6] This omission distorts policy priorities in two important ways. First, it promotes a myopic focus on compliance among those who do claim the credit, while ignoring the problem of parents who qualify but do not apply. Overzealous compliance actions can reduce uptake among people who are actually eligible.[7] Second, ignoring incomplete take-up overestimates the cost of CTC errors. Perfect taxpayer compliance would reduce incorrect CTC claims, but also increase claims from people who fail to claim the CTC despite being eligible. As a result, perfect compliance would yield less net revenue than the improper payment rate implies.[8]

## Many improper payments are benign errors—improper payments should not be conflated with fraud

Identifying the causes of improper payments is crucial to understanding the problem. A scenario in which a malicious scammer claims children using stolen Social Security numbers leads to a fundamentally different interpretation of the severity of improper payments than a case where a child's cousin, who helps raise the child but is not technically eligible, claims the CTC. Research suggests that improper payments most often resemble the latter scenario—cases where either a close family member or someone living with the child claims the CTC without meeting the strict eligibility rules.

Research on the root causes of improper refundable credit payments focuses on the Earned Income Tax Credit (EITC). While the most recent discussions of

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[6] US Department of the Treasury. *Agency Financial Report: Fiscal Year 2019.* Washington, DC, 2019. Pg. 203 https://home.treasury.gov/system/files/236/Treasury-FY-2019-AFR-Final-111519-508-FINALrevised.pdf

[7] The IRS has recently acknowledged this: "Over-reliance on audits to resolve basic errors can lead to fewer taxpayers receiving credits and deductions for which they are eligible and thus decrease accuracy in tax administration." Werfel, Danny. Letter to Members of Congress Regarding Enforcement Efforts and Audit Disparities. Internal Revenue Service, September 18, 2023. https://www.irs.gov/pub/newsroom/091823-letter-to-congress-audit-disparity.pdf

[8] The IRS tax gap report estimates $17 billion CTC payments were incorrect and a recent IRS-Census report on CTC uptake in estimated $9.3 billion of CTC was unclaimed by eligible families (both statistics include both refundable and nonrefundable portions of the credit). Coleman, Ciyata, Charles Hokayem, Sanghun Eric Kim, Ethan Krohn, Krishnan Patel, and Dean Plueger. *CTC and ACTC Participation Results and IRS-Census Match Methodology, Tax Year 2020*. No. 24-76. 2024. https://www.irs.gov/pub/irs-soi/24rpctcunderclaimsty2020census.pdf ; Internal Revenue Service. *Federal Tax Compliance Research: Tax Gap Projections for Tax Year 2022*. Publication 5869. Washington, DC: Department of the Treasury, October 2023. https://www.irs.gov/pub/irs-pdf/p5869.pdf

fraud have centered around the refundable portion of the Child Tax Credit, the EITC is a larger credit with similar claiming rules, and it has faced similar criticisms about high improper payment rates.[9] According to the Treasury Inspector General, "IRS enforcement data show the root causes of improper ACTC payments [Additional Child Tax Credit, the technical name for the refundable part of the Child Tax Credit] are similar to those of the EITC."[10]

To qualify for the CTC and EITC, claimants must meet income requirements and have a qualifying familial relationship and shared residence with the child. Research shows that most improper EITC payments result from failing the relationship or residency tests.[11] However, individuals who fail these tests are rarely strangers to the child claimed. In the vast majority of cases where EITC recipients fail the relationship or residency tests, they do have some close familial relationship or live with the child that they claim.[12] Only one percent of children associated with EITC claims had no close familial or residential connection to the filer.[13]

Other research has that shown technically incorrect EITC claims still go to low-income families. In fact, the credit has the same anti-poverty impact when accounting for true receipt (which includes technically improper claims) as simulations assuming only eligible people receive it.[14]

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[9] House Republican Policy Committee. *End Abuse of the Earned Income Tax Credit.* Guide to the Issues. Washington, DC: US House of Representatives, 2020 https://republicanpolicy.house.gov/sites/evo-subsites/republicanpolicy.house.gov/files/documents/21%20-%20End%20Abuse%20of%20the%20Earned%20Income%20Tax%20Credit.pdf

[10] Treasury Inspector General for Tax Administration. *Existing Compliance Processes Will Not Reduce the Billions of Dollars in Improper Earned Income Tax Credit and Additional Child Tax Credit Payments*. Reference Number: 2014-40-093. September 29, 2014. https://www.treasury.gov/tigta/auditreports/2014reports/201440093fr.pdf

[11] Or, when multiple people pass the relationship and shared residency tests, failing the tiebreaker tests. While some EITC errors are driven by income misreporting, this is a more general problem with tax code compliance rather than something specific to the EITC. Internal Revenue Service. *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006–2008 Returns* Publication 5162 (8-2014). Washington, DC: Department of the Treasury, August 2014. https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf

[12] For the vast majority of incorrect claims, the credit could not have been claimed by a parent. In other words, improper claims do not block correct claims by parents.

[13] It is likely some fraction of these audited EITC claimants may have not been able to document their shared residency or familial relationship with the child claimed. Leibel, Kara, Emily Y. Lin, and Janet G. McCubbin. *Social welfare considerations of EITC qualifying child noncompliance*. US Department of the Treasury, Office of Tax Analysis, 2020.

[14] Simulations of the anti-poverty impact of the EITC overstate the impact of the credit by assuming complete take-up among eligible people, but underestimate impact by

Other forms of tax noncompliance can be far more malicious. When businesses do not pay the taxes as they owe, they gain an unfair competitive advantage. For instance, the Government Accountability Office has found that federal contractors who have not paid all the taxes they owe win bids over tax-compliant contractors because not avoiding taxes allows businesses to offer lower prices.[15] Improper CTC payments are also completely unrelated to organized benefit fraud by criminal groups, such as some unemployment insurance fraud during the pandemic or the recent proliferation of stolen SNAP benefits via skimming EBT cards.

assuming only eligible people receive the credit (and there are no improper claims). The authors find these issues offset one another. Jones, Maggie R., and James P. Ziliak. "The antipoverty impact of the EITC: New estimates from survey and administrative tax records." *National Tax Journal* 75, no. 3 (2022): 451-479.

[15] US Government Accountability Office. *Financial Management: Thousands of GSA Contractors Abuse the Federal Tax System*. Testimony before the Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs, US Senate. GAO-06-492T. Washington, DC: March 14, 2006. https://www.gao.gov/assets/gao-06-492t.pdf

# Many Solutions to Improper Refundable Credit Claims Are Misguided

Concerns about improper CTC claims have inspired a range of proposed policy solutions, most of which are misguided. Some reforms would impose burdensome requirements on low-income families, while others would formally exclude children from eligibility who can receive the credit under status quo law.

### Audits may deny rightful claims and cannot be scaled up

The IRS's main solution to improper payments of refundable tax credits like the CTC is to audit claimants. While audits may seem like a cost-effective compliance measure, they cannot be scaled up and likely cause a substantial fraction of rightful claimants to have their claims denied.

The IRS audits the bulk of refundable credits via "correspondence" audits. This means mailing notices to taxpayers requiring further documentary proof that they are eligible for the credit they claimed. While over half of audited EITC returns were prepared by a paid tax preparer, just three percent of EITC claimants had professional representation during the audit process.[16] If a taxpayer has a question about their notice, they must rely on a general phone number that has a level of service of just 40 percent, meaning over half the time, these calls are not answered. Many taxpayers may not receive their audit notice at all; low-income families frequently move, and the IRS considers it sufficient to mail a notice to the taxpayer's last known address, even if it is returned as undeliverable. In contrast, audits of higher-income taxpayers are generally "field" or "office" audits. These taxpayers get a designated IRS employee as a point of contact, and taxpayers who cannot be initially reached get extensive follow-up efforts from the IRS to track them down.[17]

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[16] EITC returns not prepared by a paid tax professional likely used simple tax preparation software to prepare their return. There is no such easy to use software equivalent when responding to an audit. Taxpayer Advocate Service. *EITC Audits: What You Need to Know*. National Taxpayer Advocate Blog, August 2023. [https://www.taxpayeradvocate.irs.gov/news/nta-blog/nta-blog-eitc-audits-what-you-need-to-know/2023/08/](https://www.taxpayeradvocate.irs.gov/news/nta-blog/nta-blog-eitc-audits-what-you-need-to-know/2023/08/)

[17] Taxpayer Advocate Service. *Correspondence Audits: Low-Income Taxpayers Encounter Communication Barriers That Hinder Audit Resolution, Leading to Increased Burdens and Downstream Consequences for Taxpayers, the IRS, TAS, and the Tax Court.* In *2021 Annual Report to Congress,* Most Serious Problem #9. Washington, DC: Internal Revenue Service, 2022.

For people who receive and understand their auditing notice, substantiating a claim requires strict documentation that can be difficult to obtain. For instance, a grandmother claiming her son's child would have to produce proof that the child she claimed was her grandchild, likely via birth certificates for both her adult child and her grandchild.[18] If the grandmother's son did not appear on the birth certificate for his child, it is unlikely she would be able to substantiate her claim and would likely have to repay the credit. Claimants can have a similarly difficult job proving their child lived with them for more than half the year.[19]

Second, even if current audit practices are deemed acceptable, they cannot be scaled up to significantly reduce improper payments. Refundable credit claimants are already audited disproportionately: EITC recipients (the one refundable tax credit for which the IRS discloses audit rates) are audited five times more frequently than all other taxpayers.[20] However, overall audit rates are low.[21] This allows the IRS to focus audits on people they are most confident (using the data they have available) will fail the audit. If the IRS increased the number of audits they conducted, they would not be able to exclusively target people that they are confident would fail an audit. This approach would both burden compliant taxpayers with unnecessary audits and reduce the cost-effectiveness of enforcement efforts, as the IRS would

https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2022/01/ARC21_MSP_09_Correspondence.pdf

[18] The IRS advises EITC claimants to submit a birth certificate, paternity report, document from a court or agency, or adoption papers to substantiate being your child's parent and then the same set of documents to prove your grandchild is their child. Internal Revenue Service. Form 886-H-EIC: Documents You Need to Send to Claim the Earned Income Credit on the Basis of a Qualifying Child or Children for Tax Year 2022. Department of the Treasury, October 2022. https://www.irs.gov/pub/irs-pdf/f886he.pdf

[19] For instance, a parent with a young child not yet school-age (school records are one source of acceptable address information) and not appearing on a formal lease with their parent would likely have trouble proving their co-residency.

[20] The latest available data is for fiscal year 2022. Recently, the IRS commissioner promised to reduce audits of EITC and CTC recipients–how audits will proceed during the Trump administration is unclear. Transactional Records Access Clearinghouse (TRAC). *IRS Continues Targeting Poorest Families for More Tax Audits During FY 2022*. Syracuse University, March 29, 2022. https://trac.syr.edu/tracirs/latest/682/

[21] In Fiscal Year 2019, 0.77 percent of returns claiming the EITC were audited. *Tax Compliance: Trends of IRS Audit Rates and Results for Individual Taxpayers by Income*. GAO-22-104960. Washington, DC: May 17, 2022. https://www.gao.gov/products/gao-22-104960

spend a larger fraction of funds auditing compliant taxpayers.[22] In fact, the IRS projects reducing the improper payment rate for refundable credits below ten percent would cost the government six billion dollars.[23] It would also result in an absurd situation where low-income families are audited far more frequently than high-income taxpayers, where the bulk of noncompliance is located.[24]

**Racial and economic disparities in IRS enforcement**

Recent audit practices have been grossly inequitable. While refundable credit claimants are audited far more frequently than other taxpayers, the bulk of tax noncompliance is with higher-income groups.[25] Focusing audits on refundable credits over-polices low-income taxpayers at the expense of higher-revenue opportunities concentrating audits on wealthy households.[26]

Historical IRS audit practices have also been racially discriminatory. A team of IRS researchers and academics has estimated that Black taxpayers are audited three to five times the rate of non-Black taxpayers.[27] This pattern

[22] "The IRS would have to increase these control activities significantly in an entirely pre-refund environment to reduce the erroneous RTC payments, which would come with highly diminishing returns." US Department of the Treasury. *Agency Financial Report: Fiscal Year 2022.* Washington, DC, 2022. https://home.treasury.gov/system/files/266/Treasury-FY-2022-AFR.pdf See also: Elzayn, Hadi, Evelyn Smith, Thomas Hertz, Cameron Guage, Arun Ramesh, Robin Fisher, Daniel E. Ho, and Jacob Goldin. "Measuring and mitigating racial disparities in tax audits." The Quarterly Journal of Economics 140, no. 1 (2025): 113-163.
[23] US Department of the Treasury. *Agency Financial Report: Fiscal Year 2022.* Washington, DC, 2022.
[24] The Budget Lab. *The Revenue and Distributional Effects of IRS Funding*. Yale University, March 13, 2025. Updated April 24, 2025.
[25] According to the Yale Budget Lab's estimates of the distribution of tax noncompliance for 2025, the top 10 percent of the income distribution is responsible for eleven times more evaded taxation than the bottom 50 percent. The Budget Lab. *The Revenue and Distributional Effects of IRS Funding*. Yale University, March 13, 2025. Updated April 24, 2025. https://budgetlab.yale.edu/research/revenue-and-distributional-effects-irs-funding.
[26] Boning, William C., Nathaniel Hendren, Ben Sprung-Keyser, and Ellen Stuart. "A welfare analysis of tax audits across the income distribution." *The Quarterly Journal of Economics* 140, no. 1 (2025): 63-112.
[27] Elzayn, Hadi, Evelyn Smith, Thomas Hertz, Cameron Guage, Arun Ramesh, Robin Fisher, Daniel E. Ho, and Jacob Goldin. "Measuring and mitigating racial disparities in tax audits." *The Quarterly Journal of Economics* 140, no. 1 (2025): 113-163.

arises in large part because the IRS prioritizes detecting improper EITC payments rather than detecting the maximum amount of tax evasion.[28]

While these are problems with current audit practices, they could be fixed. In fact, the IRS pledged to remedy its racially discriminatory audits and step-up audits of high-income taxpayers during the second half of the Biden administration.[29] However, no recent data is available to see how much progress has been made on these fronts, and any policy changes may be up-in-the-air under the Trump administration.

### Restricting access to immigrant families does not reduce improper payments

The 2018 expansion of the CTC came with a new restriction—children who did not have an SSN were not allowed to be claimed for the credit. While this is a policy decision not solely motivated by integrity concerns, some Republicans have framed the Social Security Number requirement as an integrity measure. Jason Smith, Chairman of the House Ways and Means Committee, has said that "after the SSN requirement was passed in the Trump tax cuts, the improper payment rate for the CTC was cut in half."[30] In 2025, Republicans are considering requiring both children and parents claiming the credit to have an SSN, with some researchers arguing, "extending the child tax credit's SSN requirement to parents would curb fraud and improper payments."[31]

[28] While a focus on the EITC drives the bulk of the disparity, their research also found that if the IRS wanted to raise the maximum amount of revenue among improper EITC claimants, they would target far fewer Black taxpayers.
[29] Werfel, Daniel I. *Letter to Chairman Ron Wyden Regarding EITC Audit Disparities*. Internal Revenue Service, September 18, 2023. https://www.finance.senate.gov/imo/media/doc/091823_wyden_letter_from_irs_eitc_audit_disparities.pdf
[30] US House Committee on Ways and Means. *Critical Protections Against Illegal Immigrant Abuse of Tax Code Disappear If Congress Fails to Act*. December 16, 2024. https://waysandmeans.house.gov/2024/12/16/critical-protections-against-illegal-immigrant-abuse-of-tax-code-disappear-if-congress-fails-to-act/
[31] Brown, Patrick T., Josh McCabe, Leah Sargeant, David Jimenez, Ramesh Ponnuru, Brad Wilcox, Patrick Purtill, Jon Schweppe, Kristan Hawkins, Mark Rodgers, Duncan Baird, and Ivana Greco. Pro-Family Tax Provisions in 2025. October 2024. https://eppc.org/wp-content/uploads/2024/10/TCJA-Niskanen-EPPC-Memo.pdf; US House Committee on Ways and Means. *Markup of Legislative Proposals to Comply with the Reconciliation Directive Included in Section 2001 of the Concurrent Resolution on the Budget for Fiscal Year 2025, H. Con. Res. 14*. May 13, 2025.

There is no evidence that the SSN requirement reduced improper CTC payments. In fact, the CTC's improper payment rate increased 20 percent after the SSN requirement was implemented—Chairman Smith's claim that the improper payment rate was cut in half is based on his misunderstanding that improper payment statistics are reported on a lag. However, the new restriction did limit CTC eligibility for an estimated one million children.[32] The further restrictions under consideration would mean an estimated 4.5 million children lose CTC eligibility, with no evidence it would reduce improper claims.[33]

### Restricting claims to parents with legal custody would block access for rightful recipients

Commenters have called for other eligibility restrictions to bring down improper payments. One proposed reform from a Heritage Foundation report would restrict the EITC and the refundable portion of the CTC to parents with formal legal custody.[34] Similarly, a Niskanen Center report suggests that the CTC go by default to the birth parent: if someone apart from the birth parent wants to claim the CTC, they would be required to document formal custody of the child.[35]

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https://docs.house.gov/meetings/WM/WM00/20250513/118260/BILLS-119CommitteePrintih.pdf

[32] Guzman, Marco. *Inclusive Child Tax Credit Reform Would Restore Benefit to 1 Million Young 'Dreamers'*. Institute on Taxation and Economic Policy, April 27, 2021. https://itep.org/inclusive-child-tax-credit-reform-would-restore-benefit-to-1-million-young-dreamers/

[33] Lisiecki, Matthew, Danielle Wilson, Dolores Acevedo-Garcia, Sophie Collyer, Megan Curran, Joe Hughes, Emma Sifre, and Christopher Wimer. New Estimates of the Number of United States Citizen and Legal Permanent Resident Children Who May Lose Eligibility for the Child Tax Credit. Center for Migration Studies, Center on Poverty and Social Policy at Columbia University, and Institute on Taxation and Economic Policy, April 24, 2025. https://cmsny.org/wp-content/uploads/2025/05/New-Estimates-of-the-Number-of-United-States-Citizen-and-Legal-Permanent-Resident-Children-who-may-Lose-Eligibility-for-the-Child-Tax-Credit-.pdf

[34] Rector, Robert, and Jamie Bryan Hall. *Reforming the Earned Income Tax Credit and Additional Child Tax Credit to End Waste, Fraud, and Abuse and Strengthen Marriage.* Backgrounder No. 3162. Washington, DC: The Heritage Foundation, November 16, 2016. https://www.heritage.org/sites/default/files/2018-04/BG3162.pdf

[35] While the Niskanen Center report suggests defaulting the CTC to parents would reduce the burden of claiming children every year, their plan would still condition the CTC on earnings, thus requiring families to file a tax return every year. Removing the need to claim dependents on a return minimally reduces burden. McCabe, Joshua, and Leah Sargeant. *Disentangling In-Work and Child Tax Credits to Address Improper Payments: An Incremental Approach to Comprehensive Reform*. Niskanen Center, March 2025.

Requiring non-biological parents to document formal custody in order to receive the CTC may reduce improper claims, but would certainly restrict rightful incumbent recipients' eligibility for the credit. For instance, it would prohibit grandparents in multigenerational households from claiming the credit unless they have formal custody, which is unlikely if the child's parents also live in the household. Non-parents in non-traditional households may do more to raise the child than the biological parents, and (depending on specifics) they are allowed to claim the credit under current rules. Even when the "wrong" person in a multigenerational household claims the credit, these kinds of mistakes are minor technical violations—not a gross misappropriation of government funds justifying rule changes that restrict claims of caregivers currently eligible for the credit.[36]

For children not living with their biological parents, this rule would functionally disqualify many of them from receiving the CTC at all. According to the National Survey of Children in Nonparental Care, one third of children not being raised by their parents do not have formal custody arrangements.[37] Most of these children live with relatives who are currently eligible to claim the credit. The CTC and EITC already have stricter rules around family relationships for claiming children than other welfare programs like TANF and SNAP; restricting claims to parents with formal custody would further disconnect these programs' rules from the lived reality of the low-income populations they serve.[38]

https://www.niskanencenter.org/wp-content/uploads/2025/03/Disentangling-In-Work-and-Child-Tax-Credits-to-Address-Improper-Payments.pdf

[36] Research suggests low levels of "gaming" to maximize refundable credits in these kinds of households: when dependents shift between different claimants at the same address between years, one third of the time, households would have received a larger tax benefit from maintaining the same dependent assignment. Splinter, David, Jeff Larrimore, and Jacob Mortenson. "Whose Child Is This? Shifting of Dependents among EITC Claimants within the Same Household." *National Tax Journal* 70, no. 4 (2017): 737–758. https://doi.org/10.17310/ntj.2017.4.02

[37] Radel, Laura, Matthew Bramlett, Kirby Chow, and Annette Waters. *Children Living Apart from Their Parents: Highlights from the National Survey of Children in Nonparental Care.* Washington, DC: US Department of Health and Human Services, Office of the Assistant Secretary for Planning and Evaluation, May 2016. https://www.aspe.hhs.gov/sites/default/files/migrated_legacy_files/146232/NSCNC.pdf

[38] Goldin, Jacob, and Ariel Jurow Kleiman. *Whose Child Is This? Improving Child-Claiming Rules in Safety-Net Programs*. Yale Law Journal 131 (2021): 1719. https://www.yalelawjournal.org/article/whose-child-is-this

### Allowing IRS to deny claims using existing third-party data would deny rightful claims

Another seemingly anodyne reform meant to clamp down on improper payments is to deny claims that disagree with other government data. There is no comprehensive third-party database of where children live and who is taking care of them. However, various databases have at least some information on where children live. For instance, the researchers at the Niskanen Center suggest that "the IRS could cross-check data with other programs (e.g., SNAP or Medicaid) to better detect improper payments without the need for traditional audits."[39] Bipartisan Policy Center researchers have also suggested expanding the IRS's math error authority (which allows the IRS to automatically deny claims without an audit) to reduce improper refundable tax credit payments.[40]

Despite the appeal of this approach, differences between programs make it unsuitable to use other safety net programs' data to summarily deny refundable credit claims. An Urban Institute study piloting the use of SNAP data for tax credit compliance checks found that such use would require unverifiable assumptions, and concluded that "the data are unlikely suitable for use under math error authority."[41] The IRS has been through this process before with child support data. A 2001 law gave the IRS access to the Federal Case Registry of Child Support Orders, along with authority to summarily deny claims to noncustodial parents who were required to pay child support. While this may seem like a straightforward and sensible reform to cut down

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[39] McCabe, Joshua, and Leah Sargeant. *Disentangling In-Work and Child Tax Credits to Address Improper Payments: An Incremental Approach to Comprehensive Reform*. Niskanen Center, March 2025. https://www.niskanencenter.org/wp-content/uploads/2025/03/Disentangling-In-Work-and-Child-Tax-Credits-to-Address-Improper-Payments.pdf

[40] Wielk, Emily. *Improper Payments: Existing Challenges, Impact, and a Path Forward.* Washington, DC: Bipartisan Policy Center, December 2024. https://bipartisanpolicy.org/download/?file=/wp-content/uploads/2024/12/BPC_Improper-Payments-EITC-CTC-Report_R04.pdf Notably, DOGE has reportedly sought access to IRS records to check for fraud in other benefits programs. Bogage, Jacob, and Jeff Stein. "DOGE Presses to Check Federal Benefits Payments Against IRS Tax Records." *The Washington Post*, March 1, 2025. https://www.washingtonpost.com/business/2025/03/01/doge-irs-tax-records-benefits/

[41] Pergamit, Michael, Elaine Maag, Devlin Hanson, Caroline Ratcliffe, Sara Edelstein, and Sarah Minton. *Pilot Project to Assess Validation of EITC Eligibility with State Data.* Washington, DC: Urban Institute, June 3, 2015. https://www.urban.org/research/publication/pilot-project-assess-validation-eitc-eligibility-state-data

on improper payments, an IRS study found that using this data would deny claims that were actually correct 40 percent of the time.[42]

While other government data is not accurate enough for summarily denying claims, it could be useful for audit selection. However, even this approach can lead to problems. Research has found that Black taxpayers are at dramatically higher risk of being audited, and this disparity is partly attributable to third-party data being less accurate indicators of noncompliance for Black taxpayers.[43]

### Reform proposals ignore potential tradeoffs between access and integrity—some may even increase improper payments

The fact that some proposed CTC reforms would limit access for rightful recipients does not mean any effort to increase compliance with refundable tax credits is imprudent.[44] However, it illustrates that efforts to reduce improper payments often involve serious tradeoffs—proposed reforms must be carefully evaluated for both costs and benefits. Given the sparseness of evidence supporting the idea that improper CTC claims are a serious issue, any reforms should reduce improper claims with minimal burdens on rightful claimants. But many reform proposals do not even acknowledge how efforts to increase integrity can prevent some children from being rightfully claimed.

In fact, some proposed reforms may simultaneously reduce access for eligible families while increasing the rate of incorrect claims. For instance, by not allowing claims of children with SSNs from parents with ITINs, the policy increases the incentive for children to be claimed by other family members with an SSN who are not primary caregivers or who live outside the household. Similarly, defaulting claims to biological parents and putting extra

[42] Taxpayer Advocate Service. *Math Error Authority: Authorize the IRS to Summarily Assess Math and "Correctable" Errors Only in Appropriate Circumstances*. In *2015 Annual Report to Congress*, Volume 1. Washington, DC: Internal Revenue Service, 2015. https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/ARC15_Volume1_LR_02_Math-Error-Authority.pdf
[43] Hadi Elzayn, Evelyn Smith, Thomas Hertz, Cameron Guage, Arun Ramesh, Robin Fisher, Daniel E. Ho, and Jacob Goldin. "Measuring and mitigating racial disparities in tax audits." The Quarterly Journal of Economics 140, no. 1 (2025): 113-163.
[44] For instance, the IRS could improve audit practices by testing their audit selection algorithms on a small sample of claimants. With this sample, the IRS should make every effort to ensure the claims they target for audits are incorrect claims by people knowingly breaking the rules, rather than people with complicated child custody situations who may have trouble documenting their compliance. If the results show the selection algorithm is successfully targeting fraudulent claims, they could then scale-up the approach using lower-cost audit.

burdens on non-biological parents to claim the credit could plausibly increase improper payments by incorrectly issuing the credit to biological parents who are no longer primary caretakers of their children.

## Conclusion

Lawmakers' stated concerns about fraudulent refundable Child Tax Credit claims are entirely unfounded. Refundable CTC errors account for under one percent of all tax noncompliance, and the error rate is lower than the broader tax code. Even within the CTC, the refundable portion of the credit is more accurate than the nonrefundable portion that goes to middle and high-income households. Fraud is not a justifiable excuse to not expand the refundable portion of the credit.

While the CTC comprises a small amount of tax noncompliance, it has still inspired a variety of reform ideas aimed at reducing improper payments. Many of these reforms are misguided—both because they seek to resolve a tiny problem, but also because they cut off access to rightful recipients. Some proposed reforms may paradoxically reduce access for eligible families while increasing the likelihood of improper claims. As long as reforms deter more rightful claims than increase incorrect claims, they will still be scored as cost saving.

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# Appendix

### Improper payment rate calculation for the nonrefundable portion of the Child Tax Credit

The IRS reports detailed information quarterly on what fraction of the refundable portion of the CTC is paid improperly, but does not explicitly calculate an improper payment rate for the nonrefundable portion of the credit. However, as part of its tax gap analysis of noncompliance with the entire tax code, it reports the aggregate amount CTC claims contributing to overall noncompliance—including both the refundable and nonrefundable portions. It is possible to calculate the portion of incorrect payments coming from the nonrefundable portion by subtracting the portion of incorrect payments coming from the refundable portion that the IRS does explicitly report.

The IRS tax gap analysis reports the CTC contributes $17 billion to the tax gap in 2022, the latest available estimate. According to the Treasury tax expenditure report, the total CTC payments in 2022 were $101.34 billion—$36.81 billion to the refundable portion and $64.53 billion to the nonrefundable portion.[45] The IRS's latest estimate of the improper payment rate of the refundable portion of the CTC is 11 percent—making $4.05 billion of the $17 billion paid incorrectly. Subtracting the total amount of improper refundable CTC payments leaves $12.95 billion attributable to the nonrefundable portion, meaning this part of the credit has an improper payment rate of 20 percent.

A few caveats apply to this calculation. First, the CTC's improper payment rate varies every year—11 percent is not unprecedented, but it has been as high as 16 percent in the last six years. Second, the tax gap and the improper payment calculation do not use the same methodology. In particular, the $17 billion of incorrect CTC payments is a "gross tax gap" measure which does not account for any compliance efforts, while the improper payment rate calculation does account for some IRS efforts to increase compliance. While the IRS does not release a specific figure for how much of the CTC is paid out improperly after accounting for compliance efforts, adjusting for the overall ratio of pre vs. post compliance across the individual tax code would estimate the overall nonrefundable improper payment rate at 16.6 percent.

[45] U.S. Department of the Treasury. *Tax Expenditures FY2022.* Office of Tax Analysis, 2022. https://home.treasury.gov/system/files/131/Tax-Expenditures-FY2022.pdf

### Improper payment statistics erroneously overestimate noncompliance

The reported methodology used to calculate the improper payment rate for the refundable portion of the credit erroneously overestimates rates of noncompliance. Many filers who claim the CTC get only a portion of the credit as a refund, while another portion offsets tax liability. If a filer in this situation was not actually eligible to claim the credit, the IRS counts the entire amount as improper (both the refundable and nonrefundable portion) when calculating the improper payment rate. However, the improper payment rate methodology counts only the refundable portion of the credit among all taxpayers when calculating the amount of payments subject to potential errors. This effectively counts apples in the numerator and oranges in the denominator. By including amounts in the error calculation that are not counted in total payments potentially subject to error, it inevitably inflates the reported improper payment rate.

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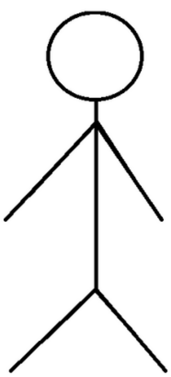
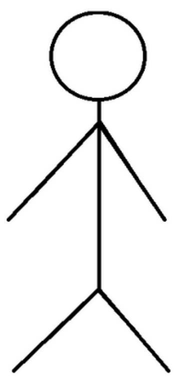
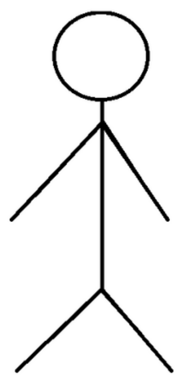
|  |  |  |
| $1,000 refundable CTC<br>$0 nonrefundable CTC | $1,000 refundable CTC<br>$0 nonrefundable CTC | $1,000 refundable CTC<br>$1,000 nonrefundable CTC |
| Correctly Claimed?<br>✅ | Correctly Claimed?<br>✅ | Correctly Claimed?<br>❌ |
| Total refundable CTC Issued = $3,000 | | |

Total refundable CTC improper, as counted by IRS methodology that counts total CTC payment if any part is refundable = $2,000
Total actual refundable CTC improper = $1,000 (the other $1,000 went to the nonrefundable portion)
Improper Payment Rate, IRS Methodology = $2,000/$3,000 = 66%
Improper Payment Rate, Corrected Methodology = $1,000/$3,000 = 33%

How much might this skew the improper payment rate? Using microsimulation, I estimate 70 percent of refundable CTC recipients get at least some fraction of the nonrefundable CTC as well. Under reasonable assumptions, if we only count the refundable part of the CTC as incorrect when calculating the improper payment rate, the portion of the payment that's incorrect would go from eleven to seven percent in fiscal year 2024.

### Incorrect improper payment rate calculation

The Treasury Department's 2019 Annual Financial Report most recently details the improper payment rate calculation methodology. They take the sum of overclaims and underpayments from randomly conducted audits, subtract that amount of incorrect CTC claims stopped via pre-refund audits, and divide by the amount of refundable credit claimed on all returns. They note that overclaims, the key quantity used in the numerator, "are based on the full amount of the RTC [refundable tax credit], including amounts used to offset reported tax liability." This means that when someone claims any amount of refundable CTC in error, their entire CTC payment, including both the refundable and nonrefundable portions, is considered incorrect. However, the denominator is "the amount of refundable credit claimed on all returns," which explicitly does not count the portion of the nonrefundable credit that many refundable credit claimants also receive.[46]

If the calculation only counted the refundable portion of the CTC as incorrect, what would the improper payment rate be? It is hard to know how much each incorrect refundable CTC claim also claimed of the nonrefundable CTC without access to the IRS audit data. However, a reasonable approach is to use the distribution of correct refundable CTC claims (from microsimulation) and assume each person has an equal chance of making an incorrect claim. This shows that, among refundable CTC claimants, for every $3 of refundable CTC claims, they also claim $2 of nonrefundable CTC. Applying this ratio to

[46] US Department of the Treasury. *Agency Financial Report: Fiscal Year 2019.* Washington, DC, 2019. https://home.treasury.gov/system/files/236/Treasury-FY-2019-AFR-Final-111519-508-FINALrevised.pdf

the improper payment rate to “scale down” the numerator, the improper payment rate goes from eleven percent to seven percent.

### Improper payment rates increased after SSN requirement was instituted

Improper payment statistics are derived from random audits of returns that claim the CTC, which take years to complete. The best estimate of the improper payment for 2018 (the first year the Tax Cuts and Jobs Act was implemented) comes from the improper payment rate calculated in 2022, as this statistic relies on 2018 audit data. Comparing improper payment rates in the years before and after the Tax Cuts and Jobs Act was implemented, the rate actually went up 20 percent.[47] Chairman Smith’s claim that the improper payment rate was cut in half when the TCJA was implemented does not account for the lagged nature of improper payment statistics, and comes from audits conducted well before the TCJA was implemented and thus do not reflect its impact. Since the improper payment rate increased after previous SSN restrictions were implemented, there is no evidence that the further restrictions being considered would improve the CTC’s integrity.[48]

### Why do improper payments get special scrutiny?

Why is the refundable portion of the child tax credit subject to special scrutiny? Part of the answer lies in special “Improper Payment Reports.” The refundable portion of the CTC (as well as other refundable credits like the EITC and the Premium Tax Credit) is subject to quarterly reports on the fraction of the credit that is “improper.” Because refundable tax credits provide a cash refund exceeding income tax liability, they are treated as a “payment” and subjected to heightened scrutiny in improper payment reports. The same reports are produced for various other payments

[47] The Treasury’s annual financial report states: “The IRS designed the initial TY 2018 NRP Individual Income Tax Reporting Compliance sample, upon which the FY 2022 estimates are based.” The increase in improper payments was not statistically significant. US Department of the Treasury. *Agency Financial Report: Fiscal Year 2022.* Washington, DC, 2022.
https://home.treasury.gov/system/files/266/Treasury-FY-2022-AFR.pdf

[48] Twenty-five years ago, the GAO reported some evidence that ITIN claims of the CTC had a higher rate of improper payments than non-ITIN claims. This predates important ITIN integrity reforms that stopped people taking advantage of the ITIN program for systematic fraud. US Government Accountability Office. *Refundable Tax Credits: Comprehensive Compliance Strategy and Expanded Use of Data Could Strengthen IRS’s Efforts to Address Noncompliance.* GAO-16-475. Washington, DC: May 2016. https://www.gao.gov/assets/gao-16-475.pdf

government agencies make, from the Department of Agriculture to the Veterans Administration.[49]

The special elevation of noncompliance with refundable tax credits in improper payment reports results in much more timely compliance data than the rest of the tax code. Improper payment reports are issued quarterly based on random audits conducted four years prior. Audits come with an inevitable time lag, so these reports give a reasonably up-to-date view on compliance with refundable tax credits. Reports on compliance with the rest of the tax code are released far more sporadically. The last two reports issued cover the periods 2014–2016, then 2020–2022. More importantly, the 2020–2022 reports rely on audits conducted for tax years 2014–2016—it simply extrapolates compliance rates for the earlier years to the distribution of tax items in later years.[50] This means that there is no estimate for how much the TCJA changed rates of tax compliance, despite being implemented for almost a decade. Such an estimate is potentially important in the debate over its renewal.

The special attention to refundable credits has no good justification. Improperly issuing a refundable credit has the same fiscal impact as failing to collect owed tax revenue. More importantly, not collecting owed tax revenue is responsible for over ten times more tax noncompliance than improperly issuing refundable credits.[51]

This differential scrutiny has an array of negative consequences. In fact, many of these negative consequences are explicitly acknowledged by the Department of Treasury under both the first Trump Administration and the Biden Administration, both of whom opposed the special improper payment calculations for refundable tax credits. For instance, the 2019 Treasury Department's annual report states that "the IRS allocates a disproportionate amount of its enforcement resources to audit returns that claim one or more [refundable tax credits]," which "runs the risk of being prevented from providing an appropriate level of enforcement in other less compliant (higher potential revenue) areas, thus reducing its overall effectiveness in maximizing

[49] This requirement stems from a unanimously passed 2020 law governing improper payment reporting, which amended prior versions of similar statutes dating back to 2002. US Congress. *Payment Integrity Information Act of 2019*. Public Law 116–117. 116th Congress, enacted March 2, 2020. https://www.congress.gov/116/plaws/publ117/PLAW-116publ117.pdf
[50] Internal Revenue Service. *Federal Tax Compliance Research: Tax Gap Projections Methodology, Tax Year 2022*. Publication 6031. Washington, DC: Department of the Treasury, 2023. https://www.irs.gov/pub/irs-pdf/p6031.pdf
[51] Internal Revenue Service. *Federal Tax Compliance Research: Tax Gap Projections for Tax Year 2022*. Publication 5869. Washington, DC: Department of the Treasury, October 2023. https://www.irs.gov/pub/irs-pdf/p5869.pdf

collections." They add that "because lower-income taxpayers make up the majority of those claiming [refundable tax credits], they are subjected to a disproportionate number of audits compared with other individual taxpayers … [creating] a burden on people with little time or money to comply with potentially expensive audits." Instead of focusing special attention and resources on refundable credit claims, they suggest that "focusing enforcement resources on the larger tax gap is a more efficient and cost-effective way to minimize the tax gap and maximize tax collections."[52]

This enormous discrepancy in bureaucratic attention spreads downstream to legislators and think tanks, where proposed reforms to credits benefiting low-income families flourish while comparatively little effort is spent on ideas to improve compliance with the rest of the tax code.[53]

[52] US Department of the Treasury. *Agency Financial Report: Fiscal Year 2019.* Washington, DC, 2019. https://home.treasury.gov/system/files/236/Treasury-FY-2019-AFR-Final-111519-508-FINALrevised.pdf

[53] While there has been ample research attention on the decaying funding for the IRS and the need to increase capacity for conducting high-income audits, there has been little attention to programmatic reforms to increase tax compliance outside of reforms to refundable credits.