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Congress Kills TCJA Kiddie Tax Changes

The Tax Cuts and Jobs Act (TCJA) changed how the tax law treated your children's investment-type income.

For some, this caused a whopping tax increase.

Now, Congress has realized the error of its ways and repealed the change—but your children have options for when they should go back to the old rules.

Sound confusing? It is. We'll make it crystal clear for you in this article.

Kiddie Tax Basics

When your children are subject to the kiddie tax, it forces them to pay taxes at a higher rate than the rate they would usually pay.

Here's the key: the kiddie tax does not apply to all of a child's income, only to his or her "unearned" income, which means income from¹

- dividends,
- rent,
- capital gains,
- interest,
- S corporation distributions, and
- any type of income other than compensation for work.

For 2019, your child pays the kiddie tax only on unearned income above \$2,100. For example, if your child has \$3,000 of unearned income, only \$900 is subject to the extra taxes.

Who Pays the Kiddie Tax?

The kiddie tax applies to children with more than \$2,100 of unearned income when the children²

- have to file a tax return,
- do not file a joint tax return,
- have at least one living parent at the end of the year,
- are under age 18 at the end of the year,
- are age 18 at the end of the year and did not have earned income that was more than half of their support, or
- are full-time students over age 18 and under age 24 at the end of the year who did not have earned income that was more than half of their support.

Calculating the Kiddie Tax

Under the TCJA, now valid only for tax years 2018 and 2019, any income subject to the kiddie tax is taxed at estate and trust tax rates, which reach a monstrous 37 percent with only \$12,070 of income in the tax year 2019.

Under the old rules before the TCJA, your child paid tax at your tax rate on income subject to the kiddie tax.

Kiddie Tax Choices

The SECURE Act, which the president signed into law on December 20, 2019, repeals the TCJA kiddie tax rules for tax years 2020 and forward and returns the tax calculation to the pre-TCJA calculation that uses your tax rate.³

The new law also gives you the option to calculate the kiddie tax using your tax rate for tax years 2018, 2019, or both—it is your choice.⁴

The IRS hasn't announced yet how your children will make this choice, but it'll likely be on Form 8615, Tax for Certain Children Who Have Unearned Income.

Takeaways

The TCJA changes to the kiddie tax hit some of your children with an outsized tax bill compared with the tax computed under the old rules.

Congress encountered resistance to the massive tax bills and decided not only to return to the old rules starting in the tax year 2020, but also to grant you the option of using the old rules for tax years 2018, 2019, or both years.

Don't forget that there are ways to defeat the kiddie tax under either the old rules or the TCJA rules. To learn the strategies, take a look at:

- Defeating the Kiddie Tax after the TCJA Tax Reform, and
- Secrets to Beating the Kiddie Tax.

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¹ IRC 1(g)(4)(A)(i); 911(d)(2).

² IRC Section 1(g)(2).

³ Pub. L. 116-94, Title V, Sec. 501.

⁴ Ibid.
