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October 26, 2009

'Kiddie tax' may close loophole, but it also hurts opportunity

Christie D'Agostini
MSU College of Law

Most of us have annoyances that seem to rattle our nerves to no end.

In the case of proactive investors, the biggest pet peeve may lie within the federal tax system - something dubbed the "kiddie tax."

This tax provision stemmed from a movement to prevent wealthy families from taking advantage of a lower tax rate on their children's unearned income.

Higher rate

The kiddie tax requires a dependent child's unearned income of more than $1,900 - up from $1,800 in 2008 - to be taxed at the higher parental tax rate of 15 percent. In 2008, the tax expanded to include college students under the age of 24 rather than children ages 18 and younger.

Unearned income in this case includes dividends, interest and capital gains.

Although Congress originally targeted the actions of wealthy families, the kiddie tax has had a broader impact.

No requirement exists within the law that calls for a qualifying income level for the kiddie tax to apply. No matter what the parents' yearend statements add up to, a dependent's unearned income is taxed at the higher rate the instant unearned income hits the $1,900 ceiling.

Discourages investing?

What about the kid who grew up in a poor household but made a decision to save and invest for his future? Surely, no intent to discourage smart investing existed when the kiddie tax was created; however, perhaps it has done exactly that.

To some, the kiddie tax is the proper screen for those looking for a loophole. But to young investors and America's future entrepreneurs, the kiddie tax is a frustrating roadblock to opportunity.

Christie D'Agostini is a second-year law student at Michigan State University's College of Law.