Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Chavez	Analyst:	Davi Milam	Bill Number:	AB 2676
Related Bills:	See Legislative History	Telephone:	845-2551	Introduced Date:	February 19, 2016
		Attorney:	Bruce Langston	Sponsor	

SUBJECT: Child & Dependent Care Expenses Credit

SUMMARY

This bill would, under the Personal Income Tax Law (PITL), increase the Child and Dependent Care Expenses Credit.

RECOMMENDATION

No position.

Summary of Suggested Amendments

An amendment has been suggested under the “Technical Considerations” section to correct a reference.

REASON FOR THE BILL

The reason for this bill is to make childcare more affordable for working families.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2016.

FEDERAL/STATE LAW

Federal Law

Existing federal law allows a tax credit of 20 to 35 percent (depending on the taxpayer's adjusted gross income (AGI)) of employment-related costs of care for a qualifying individual called the Child and Dependent Care Credit. A qualifying individual is defined as a dependent of the taxpayer that is under the age of 13 or a dependent or spouse who is physically or mentally unable to provide self-care. Employment-related expenses are generally defined as those expenses incurred to enable gainful employment. These expenses are limited to the lesser of the taxpayer’s earned income or $3,000 per taxable year for one qualifying individual, or $6,000 if there are two or more qualifying individuals.

State Law

State law allows a Child and Dependent Care Expenses Credit similar to the federal Child and Dependent Care Credit. In general, California conforms to federal law regarding qualifying individuals and the maximum amount and types of expenses eligible for the credit. However, state law limits expenses to care provided in California, and for purposes of the earned income limitation, uses earned income from California sources.

The state credit is computed by first applying the federal credit percentage (20 to 35 percent) to the smallest of three amounts: the expense cap, California expenses, or California earned income. The state credit percentage is then applied.

The state credit percentage varies based on the taxpayer's AGI[1], and is limited to taxpayers with AGI of $100,000 or less.

If AGI is:	Credit Percentage:
$40,000 or less	50%
Over $40,000 but not over $70,000	43%
Over $70,000 but not over $100,000	34%
Over $100,000	0%

THIS BILL

For taxable years beginning on or after January 1, 2016, this bill would, under the PITL, increase the child care credit by:

- Raising the AGI cap from $100,000 to $150,000; and
- Modifying the credit percentages and the AGI brackets associated with each credit percentage.

The AGI limitations and credit percentages under the terms of this bill would be:

If AGI is:	Credit Percentage:
$100,000 or less	200%
Over $100,000 but not over $125,000	100%
Over $125,000 but not over $150,000	50%
Over $150,000	0%

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[1] R&TC section 17024.5(h)(2) provides that for purposes of computing limitations, AGI means the amount required to be shown on the federal tax return for the same taxable year. In addition, for Registered Domestic Partners (RDPs) or former RDPs, AGI on the federal return is computed as if the RDP or former RDP was treated as a spouse or former spouse and used the same filing status that was used on the state tax return for the same taxable year.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would require changes to existing tax forms and instructions and information systems.

TECHNICAL CONSIDERATIONS

On page 3, line 19, the reference to IRC section 152(c)(3), relating to age requirements, should be replaced with IRC section 152(f)(1), relating to child defined.

LEGISLATIVE HISTORY

SB 268 (Nguyen, 2015/2016) would have raised the cap on expenses for the child and dependent care credit. SB 268 failed to pass the Senate Appropriations Committee by the constitutional deadline.

SB 86 (Senate Budget and Fiscal Review Committee, Chapter 14, Statutes of 2011) made the credit for child and dependent care expenses nonrefundable for taxable years beginning on or after January 1, 2011.

OTHER STATES' INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota,* and *New York.* These states were selected due to their similarities to California's economy, business entity types, and tax laws.

Florida does not have a personal income tax, and therefore does not provide a tax credit comparable to the credit this bill would allow.

Illinois, Massachusetts, and *Michigan* do not offer a child and dependent care expense credit; however, *Massachusetts* offers a deduction for child and dependent care expenses.

Minnesota and New York offer a refundable child and dependent care expense credit.

FISCAL IMPACT

The department's costs to implement this bill have yet to be determined. As the bill moves through the legislative process, costs will be identified and an appropriation will be requested, if necessary.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 2676 As Introduced February 19, 2016 Assumed Enactment After June 30, 2016 ($ in Millions)		
2016-17	2017-18	2018-19
- $160	- $160	- $170

Revenue Discussion

Using Child and Dependent Care Credit data from the IRS and department data, the amount of credit each taxpayer could claim was recalculated using the proposed credit percentages and AGI limitations. The estimated additional credit available would be $425 million as of tax year 2013. The amount of additional credit each taxpayer could use would be limited by their current tax liability. As a result, the revenue loss from the increase in the available credit is estimated to be $140 million for 2013. The estimate is then grown,[2] resulting in an estimated $155 million revenue loss in 2016. A five percent increase was added to account for dependents under age 19 with parents that never married.

The tax year estimates are converted to fiscal year estimates, and then rounded to arrive at the estimates shown in the above table.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Proponents: Some may say that in a time when many low- to middle-income working families struggle to pay for the rising cost of childcare, this credit would make childcare more affordable to these families.

Opponents: Some may argue that increasing a tax credit for low- to middle-income families may be overly narrow and inadvertently exclude other Californians that need assistance.

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[2] Indexed using the Department of Finance forecasts.

POLICY CONCERNS

For taxpayers with AGI less than $100,000, this bill would provide a state credit that is twice the amount of the federal credit. Additionally, for taxpayers with AGI of at least $100,000 and less than $125,000, this bill would provide a state credit equal to the federal credit. In general, a taxpayer's federal income tax liability is significantly higher than his or her state income tax liability. As a result, this state tax credit could be considered to provide a greater proportionate benefit for state tax purposes than for federal tax purposes.

LEGISLATIVE STAFF CONTACT

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