



## **Summary Analysis of Amended Bill**

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Sponsor:

Bill Number: AB 2023

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Amended: July 2, 2018

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Related Bills: See Prior Analysis

**Subject:** Child & Dependent Care Expenses Credit/Refundable

### **Summary**

This bill would, under the Personal Income Tax Law (PITL), make the Child and Dependent Care Expenses Credit refundable, subject to an appropriation in the annual Budget Act.

**Recommendation – No position.**

### **Summary of Amendments**

The July 2, 2018, amendments reinstated a sunset date and added limitations on the refundability of the credit.

As a result of the amendments, one of the policy concerns discussed in the department's analysis of the bill as amended May 25, 2018, and May 29, 2018, was resolved and a new implementation consideration and new technical concern were identified.

Except for the "This Bill," "Effective/Operative Date," "Implementation Considerations," "Technical Considerations," "Fiscal Impact," "Support/Opposition," and "Policy Concerns" sections, the remainder of the department's analysis of the bill as amended May 25, 2018, and May 29, 2018, still applies. The "Program Background" and "Economic Impact" sections have been restated below for convenience. The "Support/Opposition" section has been updated to reflect currently available information.

### **Effective/Operative Date**

This bill would be effective January 1, 2019, and specifically operative for taxable years beginning on or after January 1, 2019, and before January 1, 2024.

### **This Bill**

For taxable years beginning on or after January 1, 2019, and before January 1, 2024, this bill, under the PITL, would provide that if the amount of allowable Child and Dependent Care Expenses Credit exceeds the tax liability for the taxable year, the excess would be credited against other amounts due, if any, and the balance, if any, subject to the limitations below and upon appropriation by the Legislature, would be paid to the taxpayer.

The bill states that the refundable amount paid to the taxpayer would be \$0 unless otherwise specified in the annual Budget Act or any bill providing appropriations related to the Budget Act.

Under the terms of this bill, the amount paid to the taxpayer would be limited to:

- Two hundred fifty dollars (\$250) for one qualifying individual.
- Five hundred dollars (\$500) for two or more qualifying individuals.

### **Implementation Considerations**

Implementing this bill would require changes to existing tax forms and instructions, robust education and outreach, and substantial changes to information systems to limit improper payments.

Capping the refundable portion of the Child and Dependent Care Expenses Credit rather than the credit itself would add complexity for the taxpayer and the department. Additionally, the bill lacks administrative details related to the annual appropriation that would be required to pay for the refundable portion of the credit. For example:

- It is unclear when the refund and appropriation amounts would be known or whether the appropriation would be sufficient. Refunds in excess of the appropriation would be denied. This concern would be alleviated by providing for a continuous appropriation.
- By setting the refund amount at zero for years without an appropriation, the refund provision could be intermittently operative. Thus, making it unclear how the department would effectively employ staff and resources necessary to administer the refund provision. This concern could be alleviated by providing that the refund authorized by this section would only be operative for taxable years for which resources are authorized in the annual Budget Act for the Franchise Tax Board (FTB) to oversee and audit refund returns associated with this credit.

For clarity and ease of administration, the bill should be amended.

### **Technical Considerations**

For consistency of terminology, it is recommended that on page 4, line 6, the term “amount paid” be replaced with “refunded”.

### **Program Background**

#### **Legislative Analyst Office (LAO) Report**

On April 7, 2016, the LAO issued a report titled, “Options for Modifying the State Child Care Tax Credit.” This report discussed the option of restoring refundability to the State’s Child

Care Tax Credit (referred to as “Option 1”). The report also discussed the potential for improper claims, including administrative methods to limit these claims.<sup>1</sup>

### Fiscal Impact

Staff estimates startup cost of approximately \$1.7 million in fiscal year 2019/2020 and ongoing costs of approximately \$2 million each fiscal year to develop, program and test revisions to existing systems, and ongoing staffing costs. The department will pursue a budget change proposal if necessary.

### Economic Impact

#### Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 2023 as Amended on July 2, 2018  
Assumed Enactment after June 30, 2018

(\$ in Millions)

| Fiscal Year | Revenue <sup>2</sup> |
|-------------|----------------------|
| 2018-2019   | - \$33               |
| 2019-2020   | - \$55               |
| 2020-2021   | - \$55               |

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

#### Revenue Discussion

Using 2016 FTB Child and Dependent Care Expenses Credit data, it is estimated taxpayers generated approximately \$70 million in Child and Dependent Care Expenses Credit. Taxpayers applied \$31 million of the credit against their tax liabilities, leaving \$39 million in nonrefundable credits unused. The amount of refundable credit, the lesser of either \$250 or \$500 as specified in the bill or the amount of credit available, was calculated resulting in estimated tax refunds of \$34 million. The estimated credit refunded is then increased to \$55 million, to account for additional qualifying taxpayers that would file returns to claim the refundable credit. This amount was then adjusted to reflect changes over time, resulting in an estimated revenue loss from the refundable credit of \$56 million in 2019.

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<sup>1</sup> <https://lao.ca.gov/Publications/Report/3417>.

<sup>2</sup> This estimate assumes appropriation by the Legislature.

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

### **Support/Opposition<sup>3</sup>**

Support: Children's Defense Fund – California (Sponsor); Alameda County Board of Supervisors; American Academy of Pediatrics, California; California Alternative Payment Program Association, California Asset Building Coalition; California Catholic Conference; California Child Care Resource and Referral Network; California Child Development Administrators Association; Child Care Law Center; Coalition of California Welfare Rights Organizations; Equal Rights Advocates; Family Business Association; First 5 California; National Women's Law Center; Parent Voices California; San Francisco Childcare Planning and Advisory Council; Small Business Majority; Stronger California Advocates Network; Women's Foundation of California.

Opposition: None provided.

### **Policy Concerns**

The department is concerned that another refundable credit could increase the trend in refund fraud and identity theft. Historically, both the Internal Revenue Service and the FTB have experienced fraud and improper claims with refundable credits. These concerns are heightened because if a refund is determined to be fraudulent; the refund commonly cannot be recovered.

### **Legislative Staff Contact**

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<sup>3</sup> As noted in the Senate Governance and Finance Committee analysis, dated June 25, 2018.