

Author: Chavez Analyst: Davi Milam Bill Number: AB 230
Related Bills: See Legislative History Telephone: 845-2551 Introduced Date: January 26, 2017
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

REASON FOR THE BILL

The reason for this bill is to minimize the financial strains of childcare for low- to middle-income 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, 2017.

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 Expenses 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 Expenses 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 AGI¹, and is limited to taxpayers with AGI of \$100,000 or less.

<u>If AGI is:</u>	<u>Credit Percentage:</u>
\$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, 2017, this bill would, under the PITL, increase the Child and Dependent Care Expenses 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:

<u>If AGI is:</u>	<u>Credit Percentage:</u>
\$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%

IMPLEMENTATION CONSIDERATIONS

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

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.

LEGISLATIVE HISTORY

AB 2676 (Chavez, 2015/2016) would have made substantially similar changes to the Child and Dependent Care Expenses Credit as those proposed by this bill. AB 2676 failed to pass by the constitutional deadline.

SB 268 (Nguyen, 2015/2016) would have raised the cap on expenses for the Child and Dependent Care Expenses Credit. SB 268 failed to pass by the constitutional deadline.

SB 670 (Jackson, 2015/2016) would have increased the state credit percentages for the Child and Dependent Care Expenses Credit. SB 670 failed to pass by the constitutional deadline.

SB 86 (Senate Budget and Fiscal Review Committee, Chapter 14, Statutes of 2011) made the Child and Dependent Care Expenses Credit 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 expenses credit; however, *Massachusetts* offers a deduction for child and dependent care expenses.

Minnesota and New York offer a refundable child and dependent care expenses 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 230 As Introduced on January 26, 2017 Assumed Enactment After June 30, 2017 (\$ in Millions)		
2017-18	2018-19	2019-20
- \$140	- \$140	- \$140

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

Using Child and Dependent Care Expenses Credit data from the Internal Revenue Service and data from the Franchise Tax Board, the amount of credit each taxpayer would claim was recalculated using the proposed percentages and AGI limitations. The estimated additional credit available would be \$410 million as of tax year 2014. 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 \$135 million for 2014. The estimate is then adjusted to reflect changes in the economy over time, resulting in an estimated \$140 million revenue loss in 2017.

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

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.

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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