STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Santiago, et al.

Sponsor:

Bill Number: AB 1128

Related Bills: See Legislative History

Introduced: February 15, 2023

SUBJECT

Young Child Tax Credit: Qualifying Child

SUMMARY

This bill would, under the Personal Income Tax Law (PITL), expand the eligibility of the Young Child Tax Credit (YCTC) by changing the definition of a qualifying child to have the same meaning as under the California Earned Income Tax Credit (CalEITC).

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

Not applicable.

REASON FOR THE BILL

The reason for this bill is to remove the YCTC requirement that a qualifying child must be younger than 6 years of age as of the last day of the taxable year.

ANALYSIS

This bill would, under the PITL, for each taxable year beginning on or after January 1, 2023, modify the definition of a "qualifying child" by removing the criteria that the child must be younger than six years old as of the last day of the taxable year. The updated definition of a "qualifying child" would have the same meaning as under the CalEITC (Section 17052). The age criteria for a "qualifying child" for the purposes of the CalEITC requires that the individual is younger than the qualified taxpayer and either has not reached the age of 19 at the close of the tax year or has not reached the age of 24 at the close of the tax year if they are a student. Permanently and totally disabled individuals would be included as meeting the age criteria for a qualifying child for the YCTC.

This bill would also state it is the intent of the Legislature to enact subsequent legislation that would allow advance and periodic payments for the CalEITC and the YCTC at the option of the taxpayer.

This bill would also state it is the intent of the Legislature to ensure advance and periodic payments are not considered income or assets for purposes of determining eligibility for, or benefits pursuant to, any state or federal public assistance programs, or result any other negative consequences for the taxpayer, that would not occur if the taxpayer selected an annual payment.

Effective/Operative Date

This bill would be effective on January 1, 2024, and specifically operative for taxable years beginning on or after January 1, 2023.

Federal/State Law

Federal Law

Existing federal law (Internal Revenue Code (IRC) section 32) allows eligible individuals a refundable Earned Income Tax Credit (EITC). A refundable credit allows for the excess of the credit over the taxpayer's tax liability to be refunded to the taxpayer. The EITC is a percentage of the taxpayer's earned income and is phased out as income increases. For 2022, the EITC is available to individuals and families earning up to $59,187. The federal credit rate varies from 7.65% to 45%, depending on the number of qualifying children.

An eligible individual is defined as follows:

- Any individual who has a qualifying child for the taxable year, or
- Any other individual that does not have a qualifying child for the taxable year, if they meet the following requirements:
    - Has attained the age of 25 but not 65 before the close of the taxable year.
    - Has a principal place of abode in the United States for more than one-half the taxable year.
    - Not be a dependent of another taxpayer.

An eligible individual (and spouse, if filing a joint return) also must be a U.S. citizen or resident alien. If the eligible individual or spouse were a nonresident alien for any part of the tax year, the qualified individual can only claim the EITC if their filing status is married filing jointly and the individual or spouse is a:

- U.S. Citizen with a valid Social Security number (SSN), or
- Resident alien who was in the U.S. at least 6 months of the year and has a valid Social Security number.

Certain individuals are specifically excluded from the definition of an eligible individual. For example, a qualifying child, an individual who claims benefits relating to citizens or residents living abroad, a nonresident alien not treated as a U.S. resident for tax purposes.

Generally, a qualifying child must live with the eligible individual for more than one-half the taxable year in the United States, and must be under the age of 19, unless the child is a full-time student under age 24, or the child is permanently and totally disabled. Only one person can claim a qualifying child.

The name, age, and SSN of the qualifying child must be reported on the tax return.

State Law

<u>CalEITC</u>

State law provides a refundable CalEITC that is generally determined in accordance with IRC section 32, as applicable for federal income tax purposes for the taxable year, except as modified.

State law conforms to the federal definitions of an "eligible individual" and a "qualifying child" with the following exceptions:

- An eligible individual without a qualifying child must have a principal place of abode in "this state" (rather than the United States) for more than one-half of the taxable year, and for taxable years beginning on or after January 1, 2018, may have reached the age of 18 by the close of the taxable year (rather than have attained the age of 25 but not attained the age of 65 before the close of the taxable year).
- A qualifying child also must have a principal place of abode in "this state" (rather than the United States) for more than one-half of the taxable year.

The age requirement for a "qualifying child," in general, is an individual that is younger than the eligible individual claiming such individual as a qualifying child and the following applies:

- has not attained the age of 19 as of the close of the calendar year in which the taxable year of the taxpayer begins, or
- is a student who has not attained the age of 24 as of the close of such calendar year.

With regards to an individual who is permanently and totally disabled, at any time during such calendar year, the above age requirements would be treated as met.

State law conformed to the federal requirement that an eligible individual and any qualifying child must have a valid SSN. Starting in taxable years beginning on or after January 1, 2020, CalEITC eligibility is extended to individual with a taxpayer identification number (ITIN).

For purposes of the CalEITC, the federal definition of "earned income" is modified to include wages, salaries, tips, and other employee compensation, includable in federal gross income, but only if such amounts are subject to California withholding.

For 2022, the CalEITC is generally available to taxpayers with earned income of $30,000 or less.

<u>YCTC</u>

Starting in tax year 2019, a taxpayer who has been allowed the CalEITC and who has a qualifying child younger than six years old as of the last day of the taxable year may qualify for the YCTC. The maximum credit is limited to $1,000 per taxable year. The credit amount is reduced by $20 for every $100 by which the qualified taxpayer's earned income exceeds the threshold amount, initially set at $25,000. For taxable years after the minimum wage as defined by Section 1182.12 of the Labor Code is set at $15 per hour, the threshold amount will be recomputed annually in the same manner as the income tax brackets.

In addition, for taxable years beginning on or after January 1, 2022, the YCTC is also allowed to an eligible individual with a qualifying child under six years old who meets all of the following requirements:

- Would otherwise have been allowed a tax credit under Section 17052, but has earned income, as defined, of zero dollars ($0) or less.
- Does not have net losses in excess of $30,000 in the taxable year.
- Does not have wages, salaries, tips, and other employee compensation in excess of $30,000 in the taxable year.

Implementation Considerations

None noted.

Technical Considerations

In (c)(1), "For each taxable year before January 1, 2023," should be deleted and "For taxable years beginning on or after January 1, 2019, and before January 1, 2023," should be inserted to clarify the applicable start date of this provision.

In (c)(2), “For each taxable year” should be deleted and “For taxable years” should be inserted for consistency with other provisions of the Revenue and Taxation Code.

Consider removing the word "young" from the name of the credit throughout Section 17052.1.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 441 (Haney, 2023/2024) would, under the PITL, require the Franchise Tax Board (FTB) to establish a program for making advance periodic payments to qualified taxpayers allowed the CalEITC, the YCTC and the FYTC. AB 441 is currently in the legislative process.

AB 1002 (Irwin, 2023/2024) would, under the Administration of Franchise and Income Tax Laws, require the FTB to conduct a study on how to allow eligible taxpayers to claim the CalEITC, YCTC, and FYTC without filing a tax return. AB 1002 is currently in the legislative process.

AB 1355 (Valencia, 2023/2024) would, under the Administration of Franchise and Income Tax Laws, amend *The Earned Income Tax Credit Information Act* to allow for providing notifications by email. AB 1355 is currently in the legislative process.

AB 1498 (Gipson, 2023/2024) would, under the PITL, establish a minimum CalEITC, subject to appropriation, and would provide for the indexing of the minimum credit amount, and would provide for a phaseout of the minimum credit among other provisions. AB 1498 is currently in the legislative process.

SB 565 (Caballero, 2023/2024) would, under the Administration of Franchise and Income Tax Laws, require the FTB to provide a free state tax return preparation program, for qualified individuals, that utilizes prepopulated data and would allow taxpayers to edit or correct data before submitting the state return. SB 565 is currently in the legislative process.

SB 201(Committee on Budget, Chapter 72, Statutes of 2022) Section 2 of the bill, under the PITL, for taxable years beginning on or after January 1, 2022, modified the YCTC to expand the definition of a qualified taxpayer, provided for indexing of the YCTC and made other technical nonsubstantive changes.

AB 1876 (Committee on Budget, Chapter 87, Statutes of 2020) modified the CalEITC by allowing the use of federal ITINs for all eligible individuals, eligible individuals’ spouses, and qualifying children.

AB 91 (Burke, et al., Chapter 39, Statutes of 2019) enacted the California YCTC and made several changes conforming to Federal law.

SB 80 (Senate Committee on Budget and Fiscal Review, Chapter 21, Statutes of 2015) enacted the CalEITC.

AB 2589 (Santiago, et al, 2021/2022) would have, under the PITL, established a minimum CalEITC, subject to appropriation; specified the CalEITC phaseout percentages as recalculated for taxable year 2022 would apply to taxable year 2023 and later; modified the YCTC to allow an alternative computation, including expanded definitions of qualified taxpayer and qualifying child. AB 2589 did not pass out of the Senate by the constitutional deadline.

SB 860 (Rubio and Hueso, 2021/2022) would have, under the PITL, expanded the eligibility of the YCTC to individuals with zero earned income or less, required the indexing of the credit starting with taxable year 2022, required the indexing of the $20 phaseout amount for taxable year 2022 only, added additional reporting requirements for the FTB. SB 860 did not pass out of the Assembly by the constitutional deadline.

PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

This bill would impact the FTB's systems, resulting in programming and processing revisions, and form revisions as well as the need for taxpayer outreach, however the FTB's costs to implement this bill have yet to be determined. As the bill continues to move through the legislative process, costs will be determined.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 1128 as Introduced February 15, 2023
Assumed Enactment after June 30, 2023

($ in Millions)

Fiscal Year	Revenue
2023-2024	-$490
2024-2025	-$500
2025-2026	-$500

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

Based on output from the Franchise Tax Board's YCTC micro-simulation model, it is estimated that expanding the definition of a qualifying child for YCTC to that of a qualifying child for CalEITC would result in an additional revenue loss of approximately $490 million in the 2023 taxable year.

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

LEGAL IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

None noted.

ARGUMENTS

None noted.

LEGISLATIVE CONTACT

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