

Department of Legislative Services
 Maryland General Assembly
 2000 Session

FISCAL NOTE

House Bill 1013 (Delegate Shriver. *et al.*)

Ways and Means

Income Tax - Credit for Child and Dependent Care Expenses

This bill increases the State income tax credit for child and dependent care expenses from 25% to 100% of the federal child and dependent care credit and increases from \$40,000 to \$70,000 the maximum income for eligibility for the credit (from \$20,000 to \$35,000 for a married individual filing a separate return). The bill makes the credit refundable if the credit allowed exceeds the State income tax for that taxable year. The bill also alters income levels at which the credit is phased out and phase-out percentages.

The bill takes effect July 1, 2000, and applies to all taxable years beginning after December 31, 1999.

Fiscal Summary

State Effect: General fund revenue loss of approximately \$66.5 million in FY 2001 which reflects the impact of one and one-half tax years. Future years reflect 2% growth.

(in millions)	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
GF Revenues	(\$66.5)	(\$45.3)	(\$46.3)	(\$47.2)	(\$47.6)
GF Expenditures	0.0	0.0	0.0	0.0	0.0
Net Effect	(\$66.5)	(\$45.3)	(\$46.3)	(\$47.2)	(\$47.6)

Note: () = decrease; GF = general funds; FF = federal funds; SF = special funds; - =indeterminate effect

Local Effect: None. The credit is taken against the State income tax.

Small Business Effect: None.

Analysis

Current Law: The credit allowed under the State income tax for child and dependent care expenses is 25% of the federal child and dependent care credit. The maximum income for eligibility for the credit is \$40,000 and \$20,000 for a married individual filing a separate return (Chapter 584 of 1999).

Background: For federal income tax purposes, there are two existing “tax breaks” for dependent care expenses: the dependent care credit and the employer-provided dependent care spending account.

The dependent care credit is allowed for child care expenses for children through age 12 or for day care expenses for disabled spouses or dependents. The credit is allowed for up to \$2,400 in expenses for one qualified dependent and \$4,800 for two or more qualified dependents and is limited by the earned income of the taxpayer. Thus, if a parent has no earned income (a stay-home parent), the family cannot claim the credit. The credit amount is a percentage of the allowed expenses (ranging from 20% to 30%).

The employer-provided dependent care spending account allows an employee to receive up to \$5,000 tax-free each year, to be placed in a “flexible spending account” from which the employee gets reimbursed for dependent care expenses. The amount placed in a dependent care spending account reduces the amount that may be claimed under the dependent care credit, so that an individual making full use of a dependent care spending account does not get to claim the credit.

In addition to the child and dependent care credit enacted in 1999, Maryland also allows an income tax subtraction modification for qualified child and dependent care expenses of up to \$2,400 for one dependent or \$4,800 for two or more dependents. Maryland’s treatment of dependent care expenses is tied to the federal dependent care credit, in that only expenses allowed in computing the federal dependent care credit are allowed in calculating Maryland’s subtraction modification. In addition, amounts contributed to a dependent care spending account are excluded from Maryland taxable income since the starting point for determining Maryland taxable income is federal adjusted gross income (which excludes that amount).

State Fiscal Effect: According to federal income tax data for 1996, there are about 117,650 federal income tax returns from Maryland claiming the federal child care credit who could qualify under the bill for the credit. These are returns with federal adjusted gross income of \$75,000 or less claiming the federal credit for child and dependent care expenses. It is assumed that all of the Maryland residents filing federal returns taking the credit will file a Maryland return to take the State refundable credit. As a result, general fund revenue would decrease by approximately \$44.0 million in tax year 2000. Although the tax reduction applies to tax year 2000, it is assumed that for most taxpayers withholdings and estimated taxes will not be adjusted to reflect the credit until tax year 2001 because of the mid-year

effective date. Consequently, general fund revenues are estimated to decrease by approximately \$66.5 million in fiscal 2001, reflecting one and one-half tax years. The estimate assumes a growth of 2% of returns claiming the credit.

The Office of the Comptroller advises that it would incur \$33,300 in computer programming and form changes costs. The Department of Legislative Services advises that economies of scale regarding computer programming changes could be realized, since there will be change to the income tax processing system due to the 1997 income tax reduction which is phased in through 2002.

Additional Information

Prior Introductions: Chapter 584 of 1999 established a child and dependent care tax credit.

Cross File: SB 335 (Senator Van Hollen, *et al.*) - Budget and Taxation.

Information Source(s): Comptroller of the Treasury (Bureau of Revenue Estimates), Department of Legislative Services

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