SB 482

Department of Legislative Services

Maryland General Assembly
2006 Session

FISCAL AND POLICY NOTE

Senate Bill 482 (Senator Schrader, *et al.*)
Budget and Taxation

Income Tax - Subtraction Modification for Household and Dependent Care Expenses

---

This bill expands the existing subtraction modification for household and dependent care expenses by expanding eligibility of the subtraction modification for expenses incurred for any dependent under the age of 18 years old and allowing expenses paid for overnight camps for children to qualify for the subtraction modification if the expenses otherwise qualify as an employment-related expense.

The bill takes effect July 1, 2006 and applies to tax year 2006 and beyond.

Fiscal Summary

State Effect: General fund revenues could decrease by approximately $3.4 million in FY 2007 due to subtraction modifications being claimed against the personal income tax. Future years reflect estimated eligible number of taxpayers and expenses. Expenditures would not be affected.

($ in millions)	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
GF Revenue	($3.4)	($3.4)	($3.5)	($3.5)	($3.6)
Expenditure	$0	$0	$0	$0	$0
Net Effect	($3.4)	($3.4)	($3.5)	($3.5)	($3.6)

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

Local Effect: Local government revenues would decrease by approximately $2.1 million in FY 2007 and by $2.3 million in FY 2011. Expenditures would not be affected.

Small Business Effect: None.

Analysis

Current Law: Taxpayers can qualify to claim a federal and State credit and a subtraction modification to offset the child and dependent care expenses incurred for a member of the family to work or look for work as discussed below.

Background: Under Section 21 of the Internal Revenue Code, taxpayers who have earned income and have child and dependent care expenses for qualifying persons are eligible for a credit if the expenses are incurred to enable the taxpayer to be gainfully employed or look for employment and the taxpayer maintains a residence with the qualifying person. The taxpayer, and spouse if applicable, must pay more than half of the household costs of maintaining the residence for the year. A qualifying person is a child under age 13 who can be claimed as a dependent, a disabled spouse, or any disabled person not able to care for one's self who can either be claimed as a dependent, or meets all of the requirements necessary to be claimed as a dependent except that the disabled person had more than $3,100 in gross income. In order to qualify, the payments for care must be made to an individual who cannot be claimed as a dependent. The amount of expenses eligible for the credit is $3,000 for the first qualifying person and $6,000 for two or more qualifying persons. The maximum value of the credit is 35% of qualifying expenses; subject to a maximum of $1,050 for one qualifying person and $2,100 for two or more qualifying persons. The amount of the credit decreases by 1% for each $2,000 of gross income over $15,000 until adjusted gross income reaches $43,000. The credit is 20% for gross incomes $43,000 and above. Eligible nonworking spouses are treated as earning $250 a month for one qualifying person and $500 a month if there are two or more qualifying persons.

In addition to the federal credit described above, Maryland also allows an income tax subtraction modification for qualified child and dependent care expenses of up to $3,000 for one dependent or $6,000 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 (FAGI).

The State also provides an income tax credit for child and dependent care expenses equal to 32.5% of the federal child and dependent care credit. The maximum allowable income is $50,000 ($25,000 for a married individual filing a separate return). If an individual's FAGI for the taxable year exceeds $41,000, the child and dependent care credit is reduced by 10% for each $1,000 or fraction of $1,000, by which the individual's FAGI exceeds $41,000. For a married individual filing a separate return, if the individual's

FAGI for the taxable year exceeds $20,500, the credit is reduced by 10% for each $500, or fraction of $500, by which the individual's FAGI exceeds $20,500.

Finally, Maryland taxpayers are allowed to claim an exemption for dependents. For tax year 2005, the amount of the exemption is $2,400.

A total of 40,546 taxpayers claimed a total of $7.1 million in State tax credits in tax year 2004. A total of 176,496 Maryland tax returns claimed a total of approximately $103 million in federal tax credits in tax year 2003.

State Revenues: The bill expands the existing subtraction modification effective tax year 2006. As a result, general fund revenues would decrease by approximately $3.4 million in fiscal 2007. This estimate is based on the following facts and assumptions:

- As of July 1, 2004 there were an estimated 411,305 children in Maryland age 14 to 17. The number is expected to increase by 0.4% annually from 2000 to 2010.
- The 1999 National Survey of America's Families estimated that 41% of families pay for child care during the summer. The average expenditure was $297 annually.
- Approximately one-third of school age children receive after school child care at an average cost of $22 per week in 2004.
- Children aged 14 to 17 years old are half as likely than all children to be placed in after school child care or summer child care.
- Child care costs increase by 1% annually.
- Ten percent of individuals cannot take the subtraction modification because the expenses were paid by a third party or because of limited tax liability.

Local Revenues: Local government revenues would decrease by approximately 3% of the total State subtraction modification in each year. Local revenues would decrease by approximately $2.1 million in fiscal 2007, $2.2 million annually in fiscal 2008 through 2010, and $2.3 million in fiscal 2011.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): U.S. Census Bureau, Comptroller's Office, National Survey of America's Families, National Institute on Out-of-School Time, U.S. Conference of Mayors, Department of Legislative Services

Fiscal Note History: First Reader - March 6, 2006
mam/hlb

Analysis by: Robert J. Rehrmann

Direct Inquiries to:
(410) 946-5510
(301) 970-5510