HB 1122

Department of Legislative Services

Maryland General Assembly
2008 Session

FISCAL AND POLICY NOTE

House Bill 1122 (Delegate Levi, *et al.*)
Ways and Means

Income Tax - Subtraction Modification and Tax Credit for Dependent Care Expenses - Ineligibility

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This bill provides that a parent or guardian is not eligible to receive a tax credit or subtraction modification for dependent care expenses for any dependent who fails to meet specified criteria related to homework completion, student conduct, and classroom attendance. The revenues generated by the denial of these tax benefits must be transferred to the Governor's Office of Crime Control and Prevention. The State Board of Education is required to adopt regulations to implement the bill.

The bill takes effect July 1, 2008 and applies to tax year 2009 and beyond.

Fiscal Summary

State Effect: Special fund revenues could increase by $959,800 annually beginning in FY 2010. Special fund expenditures for crime control and prevention could increase beginning in FY 2010. General fund expenditures would increase by $94,500 in FY 2010 for one-time tax form changes and computer programming expenditures at the Comptroller's Office.

(in dollars)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
SF Revenue	$0	$959,800	$959,800	$959,800	$959,800
GF Expenditure	0	94,500	0	0	0
SF Expenditure	-	-	-	-	-
Net Effect	$0	$865,300	$959,800	$959,800	$959,800

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

Local Effect: To the extent that the Comptroller denies dependent care subtraction modifications and does not include local income tax revenues in the amount distributed for crime control and prevention programs, local income tax revenues could increase beginning in FY 2010. Expenditures would not be affected.

Small Business Effect: None.

Analysis

Bill Summary: The bill provides that a parent or guardian who is eligible to claim either the tax credit or subtraction modification for dependent care expenses for any dependent can claim these tax benefits only if the child meets specified criteria related to homework completion, student conduct, and classroom attendance. The Comptroller would deny the dependent care tax credit or subtraction modification claimed on behalf of any child that the county board of education determines • was ages 5 through 20 during the school year and was in a school for more than 90 days in the academic year with an "unlawful" absentee rate of 20% or more; • did not complete the minimum amount of homework required, if the local school system has adopted a systemwide minimum homework standard; or • is suspended or expelled more than once in the academic year for disrespect, insubordination, or classroom disruption.

The State Board of Education is required to adopt regulations that establish a process for determining ineligibility and allow for a decision of a county board of education to be appealed to the State board. The revenues generated, as determined by the Comptroller, by the denial of these tax benefits are to be transferred to the Governor's Office of Crime Control and Prevention.

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. A qualifying person is a child under age 13 who can be claimed as a dependent, a disabled spouse who lived with the individual claiming the credit for more than half the year, 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 for specified exceptions. Payments made to certain relatives do not qualify for the tax credit. 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. The amount of the credit is reduced if an individual receives nontaxable dependent care benefits.

In addition to the federal credit described above, the State provides two tax benefits related to dependent care expenses. 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. 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.

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.

State Revenues: Dependent care tax benefits could be disallowed beginning in tax year 2009. As a result, special fund revenues could increase $959,800 annually beginning in fiscal 2010. This estimate is based on the following facts and assumptions:

- About 140,250 tax returns with income levels specified by the bill claimed in tax year 2005 an average dependent care subtraction modification of $3,261.
- About 38,300 tax returns claimed an average dependent care credit of $172 in tax year 2006.
- 2% of subtraction modification modifications and 8% of credits would be disallowed under the bill.

State Expenditures: The Comptroller's Office reports that it would incur a one-time expenditure increase of $94,500 in fiscal 2010 to provide for the recapture of the subtraction modification and tax credit. This includes data processing changes to the SMART income tax return processing and imaging systems and system testing.

Special fund expenditures for crime control and prevention could increase by $959,800 annually beginning in fiscal 2010. The proposed fiscal 2009 State budget includes

$39.9 million in funding for the Governor's Office of Crime Control and Prevention, of which $24.9 million is general funds. It is assumed that funds provided by denial of tax benefits would provide support for additional crime control and prevention activities and would not supplant existing general fund support for the program.

Local Fiscal Effect: The bill provides that the Comptroller determines the revenues attributable to the denial of tax benefits and distributes this revenue to a special fund for crime control and prevention programs. If the Comptroller determines that revenues only include State income tax revenues, local income tax revenues would increase by $274,000 beginning in fiscal 2010 as a result of denying subtraction modifications. If the Comptroller determines revenues include local income tax revenues and includes this amount in the annual distribution for crime control and prevention, local income tax revenues would be unchanged.

It is assumed that the additional workload generated at local boards of education could be absorbed within existing budget resources.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller's Office, Maryland State Department of Education, Department of Legislative Services

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