Bill 16

Legislative Council Staff

Nonpartisan Services for Colorado's Legislature

FISCAL NOTE

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Bill Topic: **CHILD CARE EXPENSES INCOME TAX CREDIT**

Summary of Fiscal Impact:

- ☒ State Revenue
- ☒ State Expenditure
- ☐ State Transfer
- ☒ TABOR Refund
- ☐ Local Government
- ☐ Statutory Public Entity

This bill expands the availability and value of the state's low-income child care expenses income tax credit, herein called the "alternative credit." It requires one-time implementation expenditures and decreases state revenue through FY 2028-29.

Appropriation Summary: For FY 2020-21, this bill requires an appropriation of $7,040 to the Department of Revenue.

Fiscal Note Status: This fiscal note reflects the bill draft requested by the Tax Expenditure Evaluation Interim Study Committee.

Table 1
State Fiscal Impacts Under Bill 16

		FY 2019-20 *current year*	FY 2020-21	FY 2021-22
Revenue	General Fund	($2.0 million)	($4.1 million)	($4.1 million)
Expenditures	General Fund	-	$7,040	-
Transfers		-	-	-
TABOR Refund	General Fund	($2.0 million)	($4.1 million)	($4.1 million)

Summary of Legislation

Under current law, Colorado offers two tax credits for child care expenses. One credit (hereafter "traditional credit") is equal to 50 percent of the federal child and dependent care tax credit for taxpayers with adjusted gross income of $60,000 or less. A second credit (hereafter "alternative credit") is available through 2028 only to taxpayers with adjusted gross income of $25,000 or less, and is equal to 25 percent of the taxpayer's child care expenses, up to $500 if the taxpayer has one qualifying dependent or $1,000 if the taxpayer has two or more qualifying dependents. The alternative credit is available only to taxpayers who cannot claim the traditional credit because they have no federal taxable income.

Beginning in tax year 2020, this bill broadens eligibility for the alternative credit as follows:

- the adjusted gross income ceiling below which a taxpayer may qualify for the alternative credit is increased from $25,000 to $35,000;
- qualifying taxpayers who would receive a greater benefit from the alternative credit than from the traditional credit are allowed to take the alternative credit, provided that they do not also take the traditional credit; and
- the maximum alternative credit amount is increased from $500 to $525 for taxpayers with one qualifying dependent and from $1,000 to $1,050 for taxpayers with two or more qualifying dependents.

Background

Auditor's evaluation. Pursuant to Senate Bill 16-203, the Office of the State Auditor published its evaluation of the two child care expenses income tax credits in January 2019. The evaluation is available online here: https://leg.colorado.gov/sites/default/files/2019-te5_child_care.pdf.

Federal child and dependent care tax credit. Federal law allows taxpayers a nonrefundable child and dependent care tax credit against their federal income tax liability. The credit amount is equal to a percentage of qualifying care expenses, ranging from 35 percent for taxpayers with adjusted gross income of $15,000 or less to 20 percent for taxpayers with adjusted gross income over $43,000. The credit is nonrefundable, meaning it is limited by a taxpayer's federal tax liability.

The state's traditional credit is equal to 50 percent of the federal credit for all taxpayers with adjusted gross income of $60,000 or less. Because some taxpayers cannot claim the federal credit because they have no federal taxable income, the state currently offers an alternative credit to taxpayers with adjusted gross income up to $25,000 if they are not able to benefit from the federal credit.

Changes to federal tax law. The federal Tax Cuts and Jobs Act of 2017 (TCJA) reduced federal taxable income for most taxpayers with low incomes. Prior to the TCJA, taxpayers filing single returns were able to claim a personal exemption of $4,050 and a standard deduction of $6,350 in tax year 2017, for a total of $10,400. Taxpayers filing joint returns were able to claim two personal exemptions together worth $8,100 and a standard deduction of $12,700, for a total of $20,800. The TCJA eliminated personal exemptions and increased the value of standard deductions, such that single filers and joint filers were able to take standard deductions of $12,000 and $24,000, respectively, for tax year 2018. Standard deduction amounts are inflation-adjusted in future years.

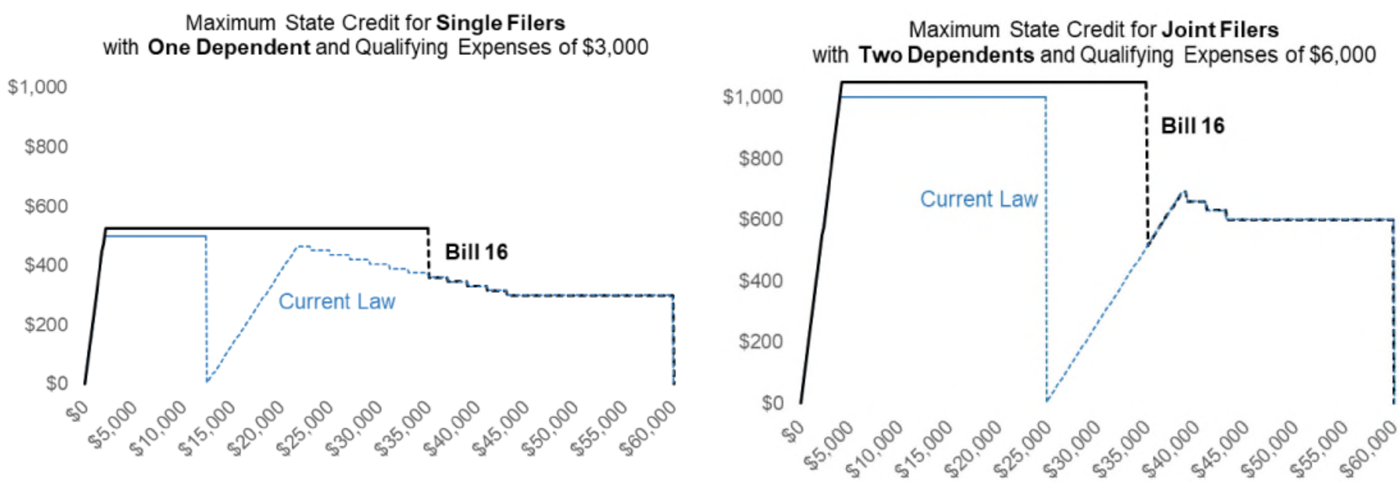
By increasing deduction amounts, the TCJA is expected to cause some joint filing taxpayers with adjusted gross income in excess of the current $25,000 ceiling for the state's alternative credit to receive a reduced benefit from the federal credit and the state's traditional credit. Under current law, in future years when the inflation-adjusted federal standard deduction exceeds $25,000, some taxpayers with incomes over $25,000 will no longer be able to benefit from either of the state's child care expenses tax credits. This population will increase as the inflation-adjusted value of the federal standard deduction increases.

State Revenue

The bill is expected to decrease General Fund revenue by $2.0 million in the current FY 2019-20, by $4.1 million in FY 2020-21 and FY 2021-22, and by a slightly greater amount in subsequent fiscal years. Revenue decreases continue through tax year 2028, at which time the alternative credit is scheduled to sunset in current law. The revenue decrease for the current FY 2019-20 represents a half-year impact for tax year 2020 on an accrual accounting basis. The bill decreases individual income tax revenue, which is subject to TABOR.

Assumptions. The bill decreases state revenue by broadening eligibility for the alternative credit and by increasing its maximum value. Both of these changes take effect in tax year 2020. Figure 1 presents changes to the maximum value of the credit for taxpayers of different adjusted gross incomes, filing statuses, and with different numbers of qualifying dependents.

Figure 1
Comparison of State Child Care Expenses Tax Credit Amounts
by Taxpayer Adjusted Gross Income under Current Law and Bill 16
Solid lines represent alternative credit; dashed lines represent traditional credit



Revenue impact estimates are based on Department of Revenue (DOR) data for actual claims of both the traditional and alternative credits for tax year 2018. The DOR data indicate that taxpayers who filed 14,035, or roughly half, of the 28,053 tax returns on which the credits were claimed would have received a larger tax credit for tax year 2018 had the changes in the bill been in effect. The total value of credits allowed to these taxpayers would increase from $3.3 million, or roughly $234 per taxpayer, to $7.4 million, or roughly $528 per taxpayer.

A significant portion of the revenue impact results because the alternative credit allows a tax benefit for a higher percentage of child care expenses than the traditional credit. By allowing taxpayers who qualify for the traditional credit to claim a larger alternative credit instead, the bill provides a benefit to taxpayers whose traditional credit amount is not constrained by their federal income tax liability. This benefit is more pronounced among taxpayers whose child care expenses are less than the maximum amount for which the federal tax credit is allowed.

Under current law, the revenue loss attributable to the traditional credit will shrink over time as more taxpayers with adjusted gross income greater than $25,000 are unable to claim the traditional credit due to insufficient federal taxable income. By allowing these taxpayers to claim the alternative credit, the bill is expected to reduce income tax revenue by an increasing amount in future years.

State Expenditures

The bill is expected to require one-time General Fund expenditures of $7,040 in FY 2020-21 only. Expenditures are summarized in Table 2 and detailed below.

Table 2
Expenditures Under Bill 16

	FY 2020-21	FY 2021-22
Department of Revenue		
GenTax Programming and Testing	$5,840	-
Form Change Cost	$1,200	-
Total Cost	**$7,040**	**-**

Department of Revenue. This bill requires changes to the DOR GenTax software system. Changes are programmed by a contractor at a rate of $250 per hour. The changes in this bill are expected to require programming expenditures of $2,000, representing 8 hours of programming. All GenTax programming changes are tested by the department. Testing for this bill will require the expenditures for contract personnel totaling $3,840, representing 160 hours of testing at a rate of $24 per hour.

The bill requires a change to one tax form at a cost of $1,200. Form changes are performed by a Department of Personnel and Administration contractor paid using reappropriated DOR funds.

TABOR refunds. The bill is expected to decrease state General Fund obligations for TABOR refunds by $2.0 million in the current FY 2019-20 and by $4.1 million in each of FY 2020-21 and FY 2021-22. Under current law and the September 2019 Legislative Council Staff forecast, the measure will correspondingly decrease the amount refunded to taxpayers in tax years 2020, 2021, and 2022.

Effective Date

The bill takes effect August 5, 2020, if the General Assembly adjourns on May 6, 2020, as scheduled, and no referendum petition is filed. The changes to the alternative credit apply beginning in tax year 2020.

State Appropriations

For FY 2020-21 only, the bill requires a General Fund appropriation of $7,040 to the Department of Revenue. From this amount, $1,200 should be reappropriated to the Department of Personnel and Administration.

State and Local Government Contacts

Information Technology Personnel Revenue State Auditor