

DEPARTMENT OF TAXATION

2017 Fiscal Impact Statement

1. **Patron** Lynwood W. Lewis, Jr.

3. **Committee** Senate Finance

4. **Title** Individual Income; Dependent Care Tax
Credit for Qualified Teachers

2. **Bill Number** SB 1531

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would allow qualified teachers to claim an individual income tax credit for household and dependent care expenses. The credit would be equal to the federal credit for child and dependent care expenses claimed on the teacher's federal tax return. This bill would impose an annual credit cap of \$1 million.

This bill would be effective for taxable years beginning on and after January 1, 2017, but before January 1, 2022.

6. **Budget amendment necessary:** No.

7. **Fiscal Impact Estimates are:** Not available. (See Line 8.)

8. **Fiscal implications:**

Administrative Costs

The Department of Taxation ("the Department") has not assigned any administrative costs to this bill because the changes required by a single bill such as this can be implemented as part of the annual changes to our systems and forms. As stand-alone legislation, the Department considers implementation of this bill as "routine," and does not require additional funding.

The Department will provide specific administrative costs on any legislation that is not "routine." Additionally, the Department will review all state tax legislation likely to be enacted prior to the passage by each house. If the aggregate number of routine bills likely to pass either house is unusually large, it is possible that additional resources will be required. If so, the Department will identify the costs at that time.

Revenue Impact

This bill would have a negative, unknown General Fund impact. According to the 2014 IRS Statistics of Income, 193,910 Virginians claimed the federal credit for child and dependent care expenses in a total amount of \$108.4 million. The average credit amount claimed by Virginians was \$559 per return.

According to the National Center for Education Statistics, Virginia had 88,070 teachers in elementary and secondary schools during the 2014 – 2015 year. Data published in 2015 by the Virginia Department of Education shows that 45.9 percent of students attend a public school where at least 40 percent of students are eligible for free or reduced lunch. Based on this, it is estimated that approximately 37,999 teachers teach in public schools where at least 40 percent of the students qualify for free or reduced lunch. If five percent of qualifying teachers were to claim the proposed tax credit at an amount equal to \$559, then the final General Fund revenue loss would likely exceed the \$1 million cap.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Federal Credit for Child and Dependent Care Expenses

Under federal law, a nonrefundable credit is allowed for a portion of qualifying child and dependent care expenses paid for the purpose of allowing the taxpayer to be gainfully employed. To be eligible for the credit, the taxpayer must incur employment-related expenses in providing care for one or more qualified individuals.

For purposes of this credit, the term “qualifying individual” means a dependent of the taxpayer who has not attained age 13; a dependent of the taxpayer who is physically or mentally incapable of caring for himself or herself and who has the same principal place of abode as the taxpayer for more than half of the taxable year; or the taxpayer’s spouse, if the spouse is incapable of caring for himself or herself and has the same principal place of abode as the taxpayer for more than half of the taxable year.

Qualifying employment-related expenses include expenses paid for household services and for the care of a qualifying individual that allow the taxpayer to work or look for work. Services rendered outside the home qualify if they involve the care of a qualified individual who regularly spends at least eight hours per day in the taxpayer’s home.

The maximum amount of employment-related expenses to which the credit may be applied is \$3,000 for one qualifying individual or \$6,000 for two or more qualifying individuals, less the amount excludable by the taxpayer for any employer-provided dependent care assistance. The amount of the credit is equal to the amount of qualified expenses multiplied by the applicable percentage, as determined by the taxpayer’s adjusted gross income (“AGI”). Taxpayer’s with an AGI of \$15,000 or less use the highest

applicable percentage of 35 percent. For taxpayers with an AGI over \$15,000, the credit is reduced by one percentage point for each \$2,000 of AGI, or fraction thereof, in excess of \$15,000. The minimum applicable percentage of 20 percent is used by taxpayers with an AGI greater than \$43,000. Thus, the maximum dependent care credit amount is \$1,050 for one qualifying individual and \$2,100 for two or more qualifying individuals.

Qualifying employment-related expenses are considered in determining the credit only to the extent of earned income. For married taxpayers, expenses are limited to the earned income of the lower-earning spouse. Generally, if one spouse is not working, no credit is allowed. However, if the nonworking spouse is physically ill or mentally incapable of caring for himself or herself or is a full-time student at an educational institution for at least five calendar months during the year, the law imputes an earned income amount, for each month of disability or school attendance, of \$250 if there is one qualifying individual or of \$500 if there is two or more qualifying individuals.

Dependent Care Federal Savings Account

A dependent care federal savings account ("dependent care FSA") is a pre-tax benefit account used to pay for eligible dependent care services, such as preschool, summer day camp, before or after school programs, and child or adult daycare. With a dependent care FSA, taxpayers can use pre-tax dollars to pay qualified out-of-pocket dependent care expenses.

In order to qualify for a dependent care FSA, a child must be under age 13 and expenses must be for before and after school care, babysitting and nanny expenses, daycare, nursery and preschool, or summer day camp. A dependent care FSA can also be used for care for a spouse or a relative who is physically or mentally incapable of self-care and lives in the taxpayer's home. The maximum contribution for a dependent care FSA is \$5,000 per year or \$2,500 per year for married taxpayers who file separate tax returns.

Virginia Deduction for Child and Dependent Care Expenses

Taxpayers may deduct the amount of employment-related expenses upon which the federal child and dependent care credit is based. The amount of employment-related expenses that may be deducted is limited to the amount actually used in computing the federal child and dependent care credit. Taxpayers are limited to a maximum deduction of \$3,000 for one child and \$6,000 for two or more dependents, or the earned income of the spouse having the lowest income, whichever is less.

The Federal Credit for Child and Dependent Care Expenses may be claimed by a taxpayer who pays expenses for the care of a qualifying individual to enable such taxpayer to be gainfully employed or actively seek employment. The amount of the Virginia deduction is based on the amount of employment-related expenses that are utilized to claim the federal credit, not the amount of the federal credit the taxpayer actually claimed (which is a percentage of his or her employment-related expenses).

Proposed Legislation

This bill would allow qualified teachers to claim an individual income tax credit for household and dependent care expenses. The credit would be equal to the federal credit for child and dependent care expenses claimed on the teacher's federal tax return. "Qualified teacher" would mean a teacher at a public elementary or secondary school in the Commonwealth at which at least 40 percent of the students qualify for free or reduced lunch. This bill would allow this credit in addition to a federal deduction for the same expenditures. There would be no prohibition on claiming another Virginia tax credit, deduction, or subtraction for the same expenses. A taxpayer would be able to take this income tax credit concurrently with the Virginia deduction for child and dependent care expenses and the federal credit for child and dependent care expenses.

This bill would impose an annual credit cap of \$1 million.

This bill would be effective for taxable years beginning on or after January 1, 2017, but before January 1, 2022.

cc: Secretary of Finance

Date: 1/25/2017 NM
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