Legislative Fiscal Bureau

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Expand Child and Dependent Care Credit
(General Fund Taxes -- Income and Franchise Taxes)

[LFB 2023-25 Budget Summary: Page 196, #7]

CURRENT LAW

Taxable income, the amount of income actually subject to tax, is calculated under current law by subtracting the state sliding scale standard deduction and personal exemptions from Wisconsin adjusted gross income (AGI). The state's marginal income tax rate and bracket schedule is then applied to taxable income to determine gross tax liability, against which eligible taxpayers may subtract any nonrefundable credits to arrive at net tax liability. Nonrefundable credits cannot be used in excess of gross tax liability.

Federal law provides a nonrefundable individual income tax credit for child and dependent care expenses that are paid for the purpose of enabling a taxpayer to be gainfully employed. The maximum amount of expenses that can be claimed for the federal credit is $3,000 if the claimant has one qualifying child (under the age of 13) or dependent (generally an individual who is physically or mentally unable to care for himself or herself) and $6,000 if the claimant has more than one qualifying child and/or dependent.

The credit is calculated as a percentage of eligible expenses, with the percentage ranging from 35% to 20%, depending on the claimant's federal AGI. For tax year 2022, the maximum reimbursement percentage of 35% begins to phase down once federal AGI exceeds $15,000. The minimum reimbursement percentage of 20% is provided once a taxpayer's federal AGI reaches $43,000.

Beginning in tax year 2022, state law provides a nonrefundable credit for child and dependent care expenses equal to 50% of the corresponding federal credit. The state credit acts as a supplement to the federal credit and reimburses between 10% and 17.5% of the claimant's eligible expenses. Together, the state and federal credits reimburse between 30% and 52.5% of eligible expenses for the first $3,000 of expenses ($6,000 for two or more children/dependents).

Eligible expenses are reduced dollar-for-dollar for any amounts excluded as dependent care assistance benefits (DCAB) under separate provisions of state and federal law. Generally, taxpayers are eligible to exclude up to $5,000 of DCAB annually. DCAB are only available to individuals if provided by a participating employer, and the employer-provided programs must satisfy certain requirements set forth under federal law.

BACKGROUND

Eligible claims for the federal credit must satisfy several tests, including a qualifying person test. Under the federal provisions, a qualifying person includes: (a) the claimant's qualifying child, who is the claimant's dependent and who was under the age of 13 when the care was provided; (b) the claimant's spouse who was physically or mentally not able to care for himself or herself and who lived with the claimant for more than half the year; and (c) a person who was physically or mentally not able to care for himself or herself, lived with the claimant for more than half the year, and, with certain exceptions, was the claimant's dependent.

The following federal tests must also be met to claim the child and dependent care credit: (a) the individual claiming the credit (and the individual's spouse, if married) must have earned income during the year (except for an individual that is a student); (b) the child and dependent care expenses must be paid so that the individual claiming the credit (and the individual's spouse, if married) can work or look for work; (c) the payments for the child and dependent care must be made to someone who cannot be claimed as a dependent of the individual claiming the credit or the individual's spouse; (d) in general, the claimant's filing status must be single, head-of-household, qualifying widow(er) with dependent child, or married-joint; and (e) the care provider must be identified on the claimant's tax return.

Prior to tax year 2022, state law provided a deduction for child/dependent care expenses based on the expenses eligible under the federal credit. Under 2021 Act 58 (the 2021-23 biennial budget act) the deduction was converted to the current credit.

Every two years, this office prepares an informational paper which reviews the individual income tax provisions in each state with such a tax. Based on that review, 28 states (including Wisconsin) provided a tax benefit based on the federal child and dependent care expenses credit in tax year 2021. Five states, including Wisconsin, offered a deduction for child and dependent care expenses based on the federal definition of eligible expenses or otherwise modeled after the federal credit (however, as noted previously, Wisconsin sunset this deduction and created the current law credit, beginning in tax year 2022). Idaho, Maryland, and Virginia structured their deduction similarly to Wisconsin's deduction. Montana allowed a deduction for individuals who care for a dependent under the age of 15, provided the individual's Montana AGI is below certain thresholds.

A credit based on the federal credit for child and dependent care expenses was offered in 24 states in tax year 2021 (including Maryland, which offered both a deduction and a credit). Generally, credits in these states are calculated either as a percentage of the federal credit or as a percentage of eligible federal expenses, although there is considerable variation in the percentages employed, and several states employ multiple percentages.

Basing the state credit on a percentage of the federal credit simplifies compliance and administration of the state tax filing system. Taxpayers need only transfer the credit amount from the relevant federal form to their state form in determining their eligible state credit amount, and state tax agencies can base administration of the credit on the federal procedures already in place.

Based on a simulation of tax year 2023 performed by the Department of Revenue (DOR), it is estimated that 107,175 filers will use total state credits of $28.9 million under current law, for an average credit of $269.

DISCUSSION POINTS

1. At public hearings on the 2023-25 biennial budget, several individuals testified about the unaffordability of child care throughout the state. Others highlighted that high costs and limited resources available to help care for elderly dependents continues to be a salient issue in Wisconsin. The child and dependent care expenses credit is designed to help individuals with dependents remain in the workforce by subsidizing the cost of caring for those dependents.

2. Moreover, slow workforce growth, an aging population of workers at or near retirement age, and limited in-migration have constrained the supply of labor in Wisconsin. By linking receipt of a tax benefit to participation in the workforce, the child/dependent care expenses credit could be viewed as a way to increase labor force participation and help mitigate workforce challenges facing Wisconsin. A Federal Reserve report from March, 2023, documented that the unaffordability and low availability of child care continues to impede labor force participation across the country.

Nonrefundable Child/Dependent Care Expenses Credit

3. To combat rising dependent care costs, and to encourage individuals to become and remain employed, the Committee could consider expanding the state credit for child and dependent care expenses to equal 100% of the corresponding federal credit, beginning in tax year 2023 [Alternative A1]. In tax year 2023, it is estimated that 103,101 filers (3.1% of all filers) would receive tax decreases totaling $27.3 million under Alternative A1, for an average decrease of $265 relative to current law. Such a proposal is included in AB 43/SB 70, and is estimated to reduce individual income tax collections by $27.3 million in 2023-24 and $27.8 million in 2024-25.

4. Under state and federal law, a taxpayer may exclude from gross income DCAB provided by a qualified dependent care benefit plan. However, a taxpayer claiming the DCAB exclusion must reduce allowable expenses under the child/dependent care expenses credit dollar-for-dollar. For many taxpayers, the value of the tax benefit they receive under the DCAB exclusion is higher than the benefit under the state and federal credits for child/dependent care expenses.

For example, in tax year 2022, a head-of-household taxpayer would be subject to a marginal federal tax rate of 22% on taxable income over $55,900. For any amount of taxable income above this amount (up to $89,050), the total value of the DCAB exclusion equaled 34.95% of eligible expenses [22% federal marginal rate + 7.65% federal payroll tax rate (Federal Insurance Contributions Act, or FICA) + 5.30% state marginal rate = 34.95%]. In other words, the tax reduction equaled 34.95 cents for every dollar of tax otherwise owed. By contrast, the same taxpayer would have received a lower tax benefit, valued at 30% of eligible expenses, if they instead claimed those expenses under the credit for child/dependent care expenses (their AGI is higher than $43,000, at which point the 20% federal/10% state credit rate is reached). The same calculations apply to married-joint filers with taxable income between $83,550 and $178,150 in tax year 2022.

As a result, many taxpayers that claim the DCAB exclusion are not able to use the full amount of child/dependent care expenses credit for which they are otherwise eligible under current law. A DOR analysis of individuals claiming the DCAB exclusion and the child/dependent care expenses credit under current law confirmed that many taxpayers claim the maximum DCAB exclusion of $5,000. Taxpayers with two or more qualifying children or dependents claim the remainder (if any, up to $1,000) of eligible expenses under the child/dependent care expenses credit, yielding a maximum combined state and federal credit of $300 under this example. Attachments 1 and 2 display the maximum and optimal mix of tax benefits available to this hypothetical taxpayer under current law.

5. From a policy perspective, it could be argued that increasing the reimbursement percentage on the same amount of expenses [as under Alternative A1] would only be successful to the extent it increases labor force participation by individuals for whom the current state credit percentage is insufficient to incent them to participate in the workforce. Otherwise, the increased reimbursement percentage under Alternative A1 would further defray expenses already occurring because current claimants would receive the enhanced credit on the first $3,000/$6,000 of expenses. However, labor force participation among individuals facing substantially higher costs for full-time child/dependent care may not significantly increase.

6. The current dollar limit under the federal credit ($3,000 for one qualifying dependent/$6,000 for two or more qualifying dependents) has not been adjusted for inflation since it was last increased in tax year 2003. For comparison, the child care advocacy organization Child Care Aware reports that the average annual cost of child care in Wisconsin in 2021 was: (a) $10,053 for a toddler/$10,840 for an infant in family child care; and (b) $11,754 for a toddler/$13,511 for an infant in center-based care.

7. To target the credit to individuals with higher expenses, and to acknowledge the impact of rising child care costs, the Committee could consider expanding the credit to an additional $7,000/$14,000 of eligible expenses, beginning in tax year 2023 [Alternative A2]. In this scenario, a taxpayer with one qualifying dependent could claim the credit for up to $10,000 of expenses that would otherwise be considered eligible under the federal credit, if not for the current law dollar limitation of $3,000. The maximum expenses would increase to $20,000 for two or more qualifying dependents. As under current law, the expenses eligible for the expanded credit would be reduced dollar-for-dollar for any amounts claimed under the DCAB exclusion. The credit rate would remain at the current law level of 50% of the federal credit the claimant could otherwise claim. Such a proposal would reduce estimated individual income tax collections by $26.7 million in 2023-24 and

$27.9 million in 2024-25.

8. Alternative A2 would differ from Alternative A1 in that it would provide a larger tax benefit to claimants with higher child and dependent care expenses. Alternative A2 would target tax benefits to individuals with young children or dependents that require full-time care in order for the individual to maintain employment. However, Alternative A2 would not provide additional tax benefits to families with child/dependent care expenses of $3,000/$6,000 or less. In tax year 2023, it is estimated that 49,933 filers (1.5% of all filers) would receive tax decreases totaling $26.7 million under Alternative A2, for an average decrease of $535 relative to current law.

9. Attachments 1 and 2 depict how the interaction under current law between the DCAB exclusion and the child and dependent care expenses credit can alter the amounts claimed under both provisions, depending on the taxpayer's circumstances. Attachment 1 displays hypothetical calculations for certain taxpayers with one child/dependent, and Attachment 2 displays those calculations for the same taxpayers with two or more children/dependents. Both attachments assume the taxpayers are subject to a top marginal federal income tax rate of 22%, claim the DCAB exclusion under current law, and incur at least $10,000 of otherwise eligible expenses per child/dependent. Under current law, the hypothetical taxpayer with one child/dependent (Attachment 1) claims no amount of child/dependent care expenses credit, and the hypothetical taxpayer with two or more children/dependents (Attachment 2) only claims $1,000 of expenses under the credit.

For the hypothetical taxpayers in Attachments 1 and 2, the optimal tax benefit for the enhanced credit under Alternative A1 would shift the allocation of expenses claimed under the credit and the DCAB exclusion, but the total amount of expenses for which preferential tax treatment is provided would not change. As a result, the optimal selection of tax benefits under Alternative A1 involves forgoing the DCAB exclusion entirely for the taxpayers with two or more children/dependents (Attachment 2), leading to a $353 increase in their optimal tax benefit relative to current law. Although the maximum combined state and federal credit for the hypothetical taxpayers with one child/dependent (Attachment 1) would increase by $300 under Alternative A1, once the reduced DCAB exclusion is taken into account, their optimal tax benefit would only result in a net tax reduction of $152.

Alternative A2 expands the total amount of expenses eligible for the child/dependent care expenses credit, so the optimal selection of tax benefits encourages these taxpayers to claim some amount of both tax benefits. Under Alternative A2, for the hypothetical filers in Attachment 1, the optimal benefit between the credit and the DCAB exclusion increases by $500 relative to current law, and for the filers in Attachment 2, the optimal benefit increases by $1,400 relative to current law. Although Alternative A2 would target tax benefits to fewer families than Alternative A1, it would provide a significantly larger benefit to families with high expenses for full-time child/dependent care.

10. In any scenario under Alternatives A1 and A2, each eligible taxpayer would need to discern their optimal tax benefit in advance, which will vary depending on their individual circumstances. For example, it may be optimal for a different filer with lower income and/or no DCAB account available to utilize the full $300/$600 increase in the state credit under Alternative A1, or the full $700/$1,400 increase in the state credit under Alternative A2, relative to current law. Moreover, taxpayers may not realize their optimal benefit under each alternative (which is partially

dependent on their income) until the close of the tax year. This is especially true for taxpayers claiming a DCAB exclusion, who must make a related election with their employer prior to the beginning of the tax year, even if the exclusion does not ultimately represent their optimal choice under Alternative A1 or A2 once the tax year has concluded. However, it should be noted that this phenomenon already exists under current law, due to the interaction between the DCAB exclusion and the state/federal credits.

Refundable Child/Dependent Care Expenses Credit

11. Some proponents of child care-related benefits may object to the fact that the tax benefits under current law and Alternatives A1 and A2 are only available to taxpayers with a net income tax liability. To expand benefits to a greater number of taxpayers, these proponents may wish to make the credit fully refundable [Alternatives A3 through A5]. Refundable credits are so named because if the credit amount exceeds the claimant's tax liability, the balance is refunded to the claimant. Unlike nonrefundable credits, refundable credits are available to individuals with no net tax liability, who tend to be lower-income individuals. In tax year 2021, for example, only 24.1% of taxpayers with Wisconsin AGI of $20,000 or less had a net tax liability. By contrast, 98.6% of taxpayers with Wisconsin AGI of $100,000 or more had a net tax liability. Refundable credits are paid from sum sufficient GPR appropriations.

12. It could be argued that a refundable credit for child and dependent care expenses [as under Alternatives A3 through A5] could act as a greater incentive for individuals without a tax liability to seek employment if they are not currently employed, or to increase hours worked if they are currently employed part-time. In both cases, the policy rationale for providing a refundable credit for child and dependent care expenses would be to further increase the supply of labor, and total state economic output, relative to a nonrefundable credit.

13. Alternative A3 would convert the current law nonrefundable credit for child and dependent care expenses to a refundable credit, beginning in tax year 2023. Alternative A3 would maintain the current reimbursement rate of 50% of the federal credit. For state budgetary and accounting purposes, nonrefundable credits are characterized as tax decreases, while refundable credits are recorded as GPR expenditures. As a result, Alternative A3 would increase individual income tax collections relative to current law by $28.9 million in 2023-24 and $29.2 million in 2024-25, but would increase state GPR expenditures by $31.5 million in 2023-24 and $31.8 million in 2024-25. The net effect of Alternative A3 on the state's general fund would be a decrease in the estimated balance of $2.6 million in 2023-24 and 2024-25. In tax year 2023, it is estimated that 10,039 filers (0.3% of all filers) would receive tax decreases totaling $2.6 million under Alternative A3, for an average decrease of $258 relative to current law.

14. Alternative A4 would adopt the Governor's proposed increase in the reimbursement rate of 100% of the federal credit (as under Alternative A1), but would make that expanded credit refundable, beginning in tax year 2023. As a result, Alternative A4 would increase individual income tax collections relative to current law by the same amount as under Alternative A3, but would increase state GPR expenditures by $62.9 million in 2023-24 and $63.6 million in 2024-25. The net effect of Alternative A4 on the state's general fund would be a decrease in the estimated balance of $34.0 million in 2023-24 and $34.4 million in 2024-25. In tax year 2023, it is estimated that 113,216 filers

(3.5% of all filers) would receive tax decreases totaling $34.0 million under Alternative A4, for an average decrease of $301 relative to current law.

15. Alternative A5 would expand the credit to the next $7,000/$14,000 of allowable expenses [as under Alternative A2], but would make the credit fully refundable, beginning in tax year 2023. As a result, Alternative A5 would increase individual income tax collections relative to current law by the same amount as under Alternatives A3 and A4, but would increase state GPR expenditures by $62.4 million in 2023-24 and $63.9 million in 2024-25. The net effect of Alternative A5 on the state's general fund would be a decrease in the estimated balance of $33.5 million in 2023-24 and $34.7 million in 2024-25. In tax year 2023, it is estimated that 61,139 filers (1.9% of all filers) would receive tax decreases totaling $33.5 million under Alternative A5, for an average decrease of $548 relative to current law.

State Child Tax Credit

16. Under current law, the child and dependent care credit is limited to an estimated 107,175 taxpayers with employment-related child and dependent care expenses in tax year 2023. The current law credit, as well as the credit proposed in Alternatives A1 through A5, is not available to families in which the caregiver refrains from seeking employment in order to provide care for a child or dependent, or to families with children who are 13 years of age or older. Relative to current law, the estimated tax benefits proposed under Alternatives A1 through A5 would be limited to between 0.3% and 3.5% of all filers in tax year 2023. One way to provide tax benefits to a greater number of families would be to extend the credit to all filers with children or dependents [Alternatives B1 and B2].

17. Based on estimates from the U.S. Department of Agriculture (USDA) adjusted for recent inflation, the estimated average cost of raising a child born in 2015 through age 17 is $18,271 annually. The USDA estimates that child care/education account for 16% of total costs, while the remaining 84% of costs are attributable to categories such as food, clothing, transportation, and health care. Based on these USDA estimates, the parent of a child under age 17 could spend an average of $15,348 per year on costs other than child care. The per-child credit under Alternatives B1 and B2 could be characterized as a way to assist parents with the significant costs of rearing a child, regardless of whether that child is placed in a formal child care setting.

18. To offset a portion of the costs associated with raising a child that are not related to child care, the federal government offers a child tax credit that may be claimed by individuals with children under 17 years of age, provided the taxpayer can claim the children as dependents. The credit equals $2,000 per child and phases out for claimants with incomes above $400,000 for married-joint filers and $200,000 for all other filers. The credit consists of both nonrefundable and refundable components. A nonrefundable credit of $500 is also provided for each of the claimant's other dependents, such as children 17 years of age or older and other relatives of the taxpayer. These provisions represent a temporary expansion of the federal credit, which was authorized under the federal Tax Cuts and Jobs Act of 2017 (TCJA) for tax years 2018 through 2025. The expansion of the credit was tied to the TCJA's elimination of personal exemptions for the same time period. The temporary nature of the expanded federal credit could be viewed as justification not to statutorily link a state child tax credit to a percentage of the federal credit.

19. Under Wisconsin's individual income tax, a $700 personal exemption is provided for each taxpayer and taxpayer's spouse, as well as for each individual claimed as a dependent. For an individual with income subject to the state's 5.30% tax rate, a $700 personal exemption equates to a $37 tax reduction. An additional $250 exemption is provided for each taxpayer who has reached the age of 65 before the end of the tax year (a $13 tax reduction if taxed at the 5.30% rate). The personal exemption for dependents is estimated to reduce individual income tax revenues by $45.9 million in tax year 2023 under current law.

20. By eliminating the personal exemption for dependents, and combining this tax savings with the $27.8 million related to the ongoing cost of the credit proposed under AB 43/SB 70 [Alternative A1], a nonrefundable state dependent tax credit of $60 per dependent could be provided, beginning in tax year 2023 [Alternative B1]. The personal exemption for filers and their spouses, and the additional personal exemption for persons 65 years of age or older, would not be eliminated as that would cause individuals without children to experience a tax increase. Similar to the federal credit, Alternative B1 would not employ an income phaseout. Incorporating an income phaseout could allow for a higher per-dependent credit rate at the same overall cost, but would also cause some taxpayers to experience a tax increase relative to current law.

21. Under Alternative B1, an estimated 709,793 filers (21.7% of all filers) would receive tax decreases totaling $29.7 million in tax year 2023, for an average decrease of $42 per taxpayer with a tax decrease. Alternative B1 would reduce individual income tax collections relative to current law by $29.7 million in 2023-24 and $30.0 million in 2024-25.

22. If the Committee desired to expand the proposed dependent tax credit to all otherwise eligible filers regardless of tax liability, it could make the credit fully refundable, beginning in tax year 2023 [Alternative B2]. Taxpayers incur costs to support children or dependents, irrespective of whether they incur a net tax liability. To keep the annual cost at a comparable level, the refundable credit could be set at $50 per dependent. As under Alternative B1, the personal exemption for dependents would be sunset beginning in tax year 2023, but the personal exemption for filers and their spouses, and the additional personal exemption for persons 65 years of age or older, would remain. In addition, the current law credit for child and dependent care expenses would be retained.

23. Alternative B2 would extend tax benefits of $29.4 million to an estimated 847,651 filers (25.9% of all filers) in tax year 2023, for an average tax decrease of $35 per taxpayer with a tax decrease. Alternative B2 would decrease individual income tax collections by an estimated $45.9 million in 2023-24 and $46.3 million in 2024-25, but would increase estimated state GPR expenditures by $75.3 million in 2023-24 and $75.8 million in 2024-25. The net effect of Alternative B2 on the state's general fund would be a decrease in the estimated balance of $29.4 million in 2023-24 and $29.5 million in 2024-25.

24. The Committee could choose to adopt one of the modifications to the current law child and dependent care expenses credit [Alternatives A1 through A5] in conjunction with a state dependent tax credit [Alternative B1 or B2], or could elect to treat each set of alternatives separately. Alternatives A1 through A5 are designed to incentivize tax filers with children or dependents to remain in the workforce by defraying some of the costs of caring for those individuals. Alternatives B1 and B2 are offered to offset other costs necessary to provide for a child or dependent (such as

food, shelter, and clothing) that exist regardless of whether that individual is employed and the child/dependent is placed in a formal care setting.

25. As a policy distinction, some tax experts object to tax credits (and tax expenditures in general) because they characterize as tax reductions what are functionally spending increases. Generally, tax credits are designed to incentivize certain behaviors. In this case, the federal child and dependent care expenses credit is primarily intended to encourage individuals with dependents to seek child care so that they can be employed. By running a credit through the income tax system to subsidize what are ultimately work-related expenses, it could be argued that the government is operating a workforce spending program by means of a tax cut via the child and dependent care expenses credit. Some argue that such an approach obscures the true nature of the tax credit as a spending program, which can then complicate lawmakers' and citizens' ability to make informed decisions on the policy merits of such a program. They might contend that, if the goal is to subsidize taxpayers with children in order for those taxpayers to be employed, a better approach might be to provide funding directly to employers so that they can provide, or otherwise subsidize, child care services for their employees. If the Committee similarly decides that an expanded tax credit for child care expenses is not the optimal way to assist parents with children to remain employed, it could decide to take no action on expanding the existing credit [Alternative A6].

26. Similarly, the Committee could determine that existing programs and tax benefits to offset the cost of raising a child/caring for a dependent are sufficient. Alternatively, the Committee could choose to separately consider a provision included in LFB Papers #363 and #366 that would increase personal exemptions (including for dependents) under current law, beginning in tax year 2023. Therefore, the Committee could elect not to create a state credit for dependents [Alternative B3].

ALTERNATIVES

A. Expand Child and Dependent Care Credit

1. Beginning in tax year 2023, expand the nonrefundable state credit for child and dependent care expenses to equal 100% of the corresponding federal credit claimed on the claimant's federal income tax return in the same tax year. Estimate reduced individual income tax collections of $27,280,800 in 2023-24 and $27,829,900 in 2024-25.

ALT A1	Change to Base
GPR-Tax	- $55,110,700

2. Beginning in tax year 2023, provide that the maximum allowable expenses under the state child and dependent care expenses credit equals $10,000 for one qualifying dependent and $20,000 for two or more qualifying dependents. Specify that the expanded credit equals 50% of the federal credit the claimant could otherwise claim if not for the $3,000/$6,000 current law expense limitation. Estimate reduced individual income tax collections relative to current law of $26,700,000

in 2023-24 and $27,900,000 in 2024-25.

ALT A2	**Change to Base**
GPR-Tax	- $54,600,000

3. Convert the current law nonrefundable credit for child and dependent care expenses to a refundable credit, beginning in tax year 2023. Maintain the current reimbursement rate of 50% of the federal credit. Increase estimated individual income tax collections relative to current law by $28,900,000 in 2023-24 and $29,200,000 in 2024-25, and increase estimated state GPR expenditures by $31,500,000 in 2023-24 and $31,800,000 in 2024-25. Estimate a net reduction in the balance of the state's general fund of $2,600,000 in 2023-24 and 2024-25.

ALT A3	**Change to Base**
GPR-Tax	$58,100,000
GPR	63,300,000

4. Adopt Alternative A1, but make the credit refundable, beginning in tax year 2023. Increase estimated individual income tax collections relative to current law by $28,900,000 in 2023-24 and $29,200,000 in 2024-25, and increase estimated state GPR expenditures by $62,900,000 in 2023-24 and $63,600,000 in 2024-25. Estimate a net reduction in the balance of the state's general fund of $34,000,000 in 2023-24 and $34,400,000 in 2024-25.

ALT A4	**Change to Base**
GPR-Tax	$58,100,000
GPR	126,500,000

5. Adopt Alternative A2, but make the credit refundable. Increase estimated individual income tax collections relative to current law by $28,900,000 in 2023-24 and $29,200,000 in 2024-25, and increase estimated state GPR expenditures by $50,400,000 in 2023-24 and $51,200,000 in 2024-25. Estimate a net reduction in the balance of the state's general fund of $21,500,000 in 2023-24 and $22,000,000 in 2024-25.

ALT A5	**Change to Base**
GPR-Tax	$58,100,000
GPR	101,600,000

6. Take no action.

B. Create State Dependent Tax Credit

1. Beginning in tax year 2023, create a nonrefundable credit equal to $60 for each dependent claimed on the taxpayer's state individual income tax return, and sunset the personal exemption for dependents. Reduce estimated individual income tax collections relative to current law by $29,700,000 in 2023-24 and $30,000,000 in 2024-25.

ALT B1	Change to Base
GPR-Tax	- $59,700,000

2. Beginning in tax year 2023, create a refundable credit equal to $50 for each dependent claimed on the taxpayer's state individual income tax return, and sunset the personal exemption for dependents. Estimate increased state individual income tax collections of $45,900,000 in 2023-24 and $46,300,000 in 2024-25, and increased GPR expenditures of $75,300,000 in 2023-24 and $75,800,000 in 2024-25. Estimate a reduction in the balance of the state's general fund of $29,400,000 in 2023-24 and $29,500,000 in 2024-25.

ALT B2	Change to Base
GPR-Tax	$92,200,000
GPR	151,100,000

3. Take no action.

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Attachments

ATTACHMENT 1

Maximum Tax Benefits for Hypothetical Head-of-Household Taxpayer with Federal AGI of $65,000, or Married-Joint Taxpayer with Federal AGI of $95,000, One Child/Dependent, Tax Year 2023

One Child or Dependent, $10,000 or More of Eligible Expenses

Current Law*		Alternative A1*		Alternative A2*	
DCAB Benefit		**DCAB Benefit**		**DCAB Benefit**	
Exclusion Amount	$5,000	Exclusion Amount	$5,000	Exclusion Amount	$5,000
FICA Tax Rate	7.65%	FICA Tax Rate	7.65%	FICA Tax Rate	7.65%
Federal Income Tax Rate	22.00	Federal Income Tax Rate	22.00	Federal Income Tax Rate	22.00
State Income Tax Rate	5.30	State Income Tax Rate	5.30	State Income Tax Rate	5.30
Total Effective Tax Rate	34.95%	Total Effective Tax Rate	34.95%	Total Effective Tax Rate	34.95%
Maximum State and Federal DCAB Benefit	$1,748	Maximum State and Federal DCAB Benefit	$1,748	Maximum State and Federal DCAB Benefit	$1,748
Child and Dependent Tax Credit		**Child and Dependent Tax Credit**		**Child and Dependent Tax Credit**	
Eligible Expenses	$3,000	Eligible Expenses	$3,000	Eligible Expenses for Federal and State Credit	$3,000
Federal Credit Percentage	20%	Federal Credit Percentage	20%	Federal Credit Percentage	20%
State Credit Percentage	10	State Credit Percentage	20	State Credit Percentage	10
Total Credit Percentage	30%	Total Credit Percentage	40%	Total Credit Percentage	30%
				Eligible Expenses for State Credit Only	$7,000
				State-Only 10% Credit	700
Maximum State and Federal Credit	$900	Maximum State and Federal Credit	$1,200	Maximum State and Federal Credit	$1,600

TAXPAYER'S OPTIMAL CHOICE OF TAX BENEFITS

Current Law*		Alternative A1*		Alternative A2*	
DCAB Benefit ($5,000 of expenses)	$1,748	DCAB Benefit ($2,000 of expenses)	$699	DCAB Benefit ($5,000 of expenses)	$1,748
Child/Dep. Benefit	0	Child/Dep. Benefit ($3,000 of expenses)	1,200	Child/Dep. Benefit ($5,000 of expenses)	500
TOTAL TAX BENEFIT	$1,748	**TOTAL TAX BENEFIT**	$1,899	**TOTAL TAX BENEFIT**	$2,248
		Change to Current Law	**$152**	**Change to Current Law**	**$500**

*Total tax benefit calculations also apply to proposed refundable credits under Alternative A3 (same as current law), Alternative A4 (same as Alternative A1), and Alternative A5 (same as Alternative A2).

ATTACHMENT 2

Maximum Tax Benefits for Hypothetical Head-of-Household Taxpayer with Federal AGI of $65,000, or Married-Joint Taxpayer with Federal AGI of $95,000, Two or More Children/Dependents, Tax Year 2023

Two or More Children or Dependents, $20,000 or More of Eligible Expenses

Current Law*		Alternative A1*		Alternative A2*	
DCAB Benefit		**DCAB Benefit**		**DCAB Benefit**	
Exclusion Amount	$5,000	Exclusion Amount	$5,000	Exclusion Amount	$5,000
FICA Tax Rate	7.65%	FICA Tax Rate	7.65%	FICA Tax Rate	7.65%
Federal Income Tax Rate	22.00	Federal Income Tax Rate	22.00	Federal Income Tax Rate	22.00
State Income Tax Rate	5.30	State Income Tax Rate	5.30	State Income Tax Rate	5.30
Total Effective Tax Rate	34.95%	Total Effective Tax Rate	34.95%	Total Effective Tax Rate	34.95%
Maximum State and Federal DCAB Benefit	$1,748	Maximum State and Federal DCAB Benefit	$1,748	Maximum State and Federal DCAB Benefit	$1,748
Child and Dependent Tax Credit		**Child and Dependent Tax Credit**		**Child and Dependent Tax Credit**	
Eligible Expenses	$6,000	Eligible Expenses	$6,000	Eligible Expenses for Federal and State Credit	$6,000
Federal Credit Percentage	20%	Federal Credit Percentage	20%	Federal Credit Percentage	20%
State Credit Percentage	10	State Credit Percentage	20	State Credit Percentage	10
Total Credit Percentage	30%	Total Credit Percentage	40%	Total Credit Percentage	30%
				Eligible Expenses for State Credit Only	$14,000
				State-Only 10% Credit	$1,400
Maximum State and Federal Credit	$1,800	Maximum State and Federal Credit	$2,400	Maximum State and Federal Credit	$3,200

TAXPAYER'S OPTIMAL CHOICE OF TAX BENEFITS

DCAB Benefit ($5,000 of expenses)	$1,748	DCAB Benefit	$0	DCAB Benefit ($5,000 of expenses)	$1,748
Child/Dep. Benefit ($1,000 of expenses)	300	Child/Dep. Benefit ($6,000 of expenses)	2,400	Child/Dep. Benefit ($15,000 of expenses)	1,700
TOTAL TAX BENEFIT	$2,048	**TOTAL TAX BENEFIT**	$2,400	**TOTAL TAX BENEFIT**	$3,448
		Change to Current Law	**$353**	**Change to Current Law**	**$1,400**

*Total tax benefit calculations also apply to proposed refundable credits under Alternative A3 (same as current law), Alternative A4 (same as Alternative A1), and Alternative A5 (same as Alternative A2).