

MINNESOTA • REVENUE

INDIVIDUAL INCOME TAX Dependent Care Credit

March 7, 2011

	Yes	No
DOR Administrative Costs/Savings	X	

Department of Revenue
Analysis of H.F. 772 (Slawik)

	<u>Fund Impact</u>			
	<u>F.Y. 2012</u>	<u>F.Y. 2013</u>	<u>F.Y. 2014</u>	<u>F.Y. 2015</u>
			(000's)	
General Fund	(\$11,900)	(\$11,600)	\$1,700	\$1,900

Effective for tax years beginning after December 31, 2010.

EXPLANATION OF THE BILL

Current Law: A Minnesota taxpayer may claim a refundable credit for a portion of dependent care expenses provided that those expenses were necessary in order to hold or look for a job. A dependent is defined as a child under age 13 or a dependent or spouse of any age who is disabled. Dependents who qualify for the federal child care credit also qualify for the Minnesota dependent care credit.

The determination of the credit starts with the federal child and dependent care credit, which is equal to eligible expenses up to \$3,000 for one dependent and \$6,000 for two or more dependents multiplied by a percentage ranging from 35% to 20%, with the percentage decreasing as income increases. Individuals with adjusted gross income under \$15,000 receive the maximum rate of 35%. The credit percentage decreases by one percentage point for each \$2,000 of income over \$15,000 to a minimum of 20% percent for individuals with income over \$43,000. The maximum federal credit in tax year 2011 is \$1,050 for one qualifying person and \$2,100 for two or more qualifying persons. The federal credit is based on adjusted gross income, is not phased out, is nonrefundable, and is only of benefit to taxpayers who have federal tax liability.

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended for two years the enhancements to the federal dependent care credit from the Tax Relief Act of 2001. As a result, for tax years 2013 and after, maximum eligible expense amounts decline from \$3,000 to \$2,400 for one dependent and from \$6,000 to \$4,800 for two or more dependents with the percentage ranging from 30% to 20%, with the rate reduction beginning at \$10,000 rather than \$15,000. At this time, Minnesota has not conformed to the extension of the federal dependent care credit enhancements for tax years 2011 and 2012.

The Minnesota credit is limited to a maximum of \$720 for one child and \$1,440 for two or more children, and the maximum state credit allowed is based on total household income. For tax year 2010 the maximum amounts were reduced for taxpayers with total household incomes over \$23,380, so that a taxpayer with total household income over \$37,030 received no credit. The threshold amount is indexed for inflation.

EXPLANATION OF THE BILL (Cont.)

Proposed Law: The proposal redefines the Minnesota dependent care credit so that it equals the amount of the federal dependent care credit that exceeds federal tax liability after deducting the federal child credit. Therefore, the Minnesota dependent care credit is equal to the unused portion of the federal credit and would remain refundable. In essence, the combination of the federal child care credit and the state dependent care credit allows the taxpayer to receive the full benefit of the federal child care credit. Since the new credit is tied to the federal credit, it does not phase out over a threshold amount and individuals who have no federal tax liability would also be eligible for the credit.

REVENUE ANALYSIS DETAIL

- The House Income Tax Simulation (HITS 5.9) Model was used to estimate the tax year revenue impact. These simulations assume the same economic conditions used by Minnesota Management and Budget for the forecast published in February 2011. The model uses a stratified sample of 2008 individual income tax returns compiled by the Minnesota Department of Revenue.
- Due to the reversion of the federal tax code to pre-2001 law in tax year 2013, the amount of the credit drops in 2013 and succeeding years.
- The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 temporarily extended for two years the \$1,000 per child federal child credit. For tax years 2013 and after, the federal child credit reverts to \$500 per child.
- Tax year impact would be reflected in the following fiscal year.

Number of Taxpayers: In tax year 2011, the credit would increase on 42,800 returns and decrease on 5,400 returns. The number of returns that would receive the state credit would have a net increase of 9,800 returns. In tax year 2013, the credit would increase on 6,000 returns and decrease on 16,500 returns. The number of returns that would receive the state credit would have a net decrease of 7,500 returns.

Source: Minnesota Department of Revenue
Tax Research Division
http://www.taxes.state.mn.us/taxes/legal_policy