

DAVID Y. IGE
GOVERNOR

JOSH GREEN M.D.
LT. GOVERNOR



STATE OF HAWAII
DEPARTMENT OF TAXATION
P.O. BOX 259
HONOLULU, HAWAII 96809
PHONE NO: (808) 587-1540
FAX NO: (808) 587-1560

RONA M. SUZUKI
DIRECTOR OF TAXATION

DAMIEN A. ELEFANTE
DEPUTY DIRECTOR

To: The Honorable Donovan M. Dela Cruz, Chair;
The Honorable Gilbert S.C. Keith-Agaran, Vice Chair;
and Members of the Senate Committee on Ways and Means

From: Rona M. Suzuki, Director
Department of Taxation

Re: S.B. 2283, Relating to Taxation

Date: Thursday, February 13, 2020

Time: 11:00 A.M.

Place: Conference Room 211, State Capitol

The Department of Taxation (Department) offers the following comments regarding S.B. 2283.

S.B. 2283 creates a refundable income tax credit equal to an unspecified percentage of eligible child care expenses during the taxable year.

The Department notes that a tax credit for child care expenses already exists under Hawaii Revised Statutes (HRS) section 235-55.6. That section provides a refundable income tax credit for expenses for household and dependent care necessary for gainful employment and would apply to expenses paid for child care. If the Committee wishes to amend or expand the State's existing tax incentives for child care, the Department suggests doing so by amending HRS section 235-55.6 rather than creating a new tax credit.

Thank you for the opportunity to provide comments.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: NET INCOME, Refundable Child Care Expense Credit Taxation

BILL NUMBER: SB 2283

INTRODUCED BY: DELA CRUZ

EXECUTIVE SUMMARY: Establishes a child care expense refundable tax credit that is equal to an unspecified per cent of the amount the taxpayer spent on eligible child care expenses during that taxable year. Defines "eligible child care expenses" as the total amount the taxpayer paid to a child care facility in the State for the care of a child who is under the age of 13 and for whom the taxpayer is entitled to a deduction under section 235-54(a), HRS. Prohibits a taxpayer from claiming both the child care expenses tax credit and the credit for employment-related expenses for household and dependent care services under section 235-55.6, HRS. Applies to taxable years beginning after December 31, 2019.

SYNOPSIS: Adds a new section to chapter 235, HRS, to allow a refundable child care expense tax credit equal to ___% of the taxpayer's eligible child care expenses during the taxable year.

Defines "eligible child care expenses" as the total amount of money the taxpayer paid to a licensed child care facility in the State during the taxable year for the care of a child: (1) who is under the age of thirteen; and (2) for whom the taxpayer is entitled to a personal exemption for income tax purposes.

All claims, including amended claims, for a tax credit shall be filed on or before the end of the twelfth month following the close of the taxable year. Failure to comply with the foregoing provision shall constitute a waiver of the right to claim the credit.

States that no other tax credit or deduction shall be claimed under this chapter for the certain expenses used to claim a tax credit under this section for the taxable year.

States that a taxpayer shall not be eligible to claim a tax credit under this section if the taxpayer is claiming a credit under section 235-55.6 (credit for expenses for household and dependent care services necessary for gainful employment).

EFFECTIVE DATE: Taxable years beginning after December 31, 2019.

STAFF COMMENTS: There are some issues to consider with refundable credits targeted at low-income and homeless people generally and with the proposed credit in particular.

First, a tax return is one of the most complicated documents for government agencies to process. The administrative costs associated with each one can quickly make heads spin. Furthermore, as the U.S. Treasury has experienced with the Earned Income Tax Credit, the combination of complexity and a refundable credit result in a certain percentage of improper payouts, some due to mistake or misunderstanding, and some due to bad actors.

Second, the credit as proposed overlaps, as the bill recognizes, with the existing credit for expenses for household and dependent care services necessary for gainful employment. This overlap inevitably will cause some taxpayers to claim one credit while being entitled to the other, and the foot fault could well result in disallowance of both credits. For example, suppose a divorced taxpayer with a child that spends some time out of state with a former spouse is under child support obligations and incurs expenses for a child care facility out of state. Those expenses would be eligible for the existing credit but are not eligible for the new one. If the taxpayer claims the credit under this bill, and is audited a year later, the credit will be disallowed (a child care facility in Hawaii is required) and it will be too late to claim the proper credit (more than 12 months after the close of the taxable year in which expenses were incurred).

Third, even for those in the target population who do qualify for this credit, the relief that the credit provides comes in a tax refund which is paid, at the earliest, in the early part of the year after the tax return filer needs the relief. A person who qualifies for the credit in 2017, for example, won't get a check until early 2018.

Fourth, as a policy matter, lawmakers might prefer that the recipient of the refund not use the money obtained on certain things, illegal drugs for example. But the tax system contains no way of restricting the uses of a refund check; other departments do have systems in place to give some assurance that the payment will go toward legitimate living expenses such as groceries (EBT, for example).

The better solution is to get such people out of the tax system entirely. They receive peace of mind because they don't have to worry about tax returns, and the department doesn't have to worry about processing those returns. If additional relief to such people is considered desirable, it can be delivered through the agencies that are better equipped to do so.

Indeed, the Foundation has recently written about the TANF (Temporary Assistance for Needy Families) program, where Hawaii so far has left \$281 million of federal money on the table and is not up to par with other states in providing child care subsidies. A reprint of the article (published Dec. 2, 2019) follows:

TANF: \$281M Federal Money We Haven't Spent

This week we focus on our safety net systems for people or families in need. In the early 1990s, a major part of this net came from the federal Aid to Families with Dependent Children (AFDC) program, which matched state dollars of financial assistance for a needy family. That program was replaced with what we have now, Temporary Assistance for Needy Families (TANF), which is a federal block grant program that, at least in theory, gives states a substantial amount of federal money for purposes like cash assistance, work activities, work supportive services, and child care.

Hawaii gets about [\\$99 million a year](#) under this program. In 2017, it spent \$52 million in federal funds while it spent about three times that amount from its own funds.

That means there was \$47 million in federal money left over just from that year. A state can (at least for now) carry the money over to future years, but...as of last year, [Hawaii](#)

[had \\$281 million](#) in unspent TANF money. That means our state was underutilizing this money on a consistent, year-to-year basis.

A post on the website [efficient.gov](#) quotes an assistant division administrator for the Department of Human Services as saying, “I’m concerned the reserve is larger than it needs to be. I do worry that if we don’t spend it, then our clients aren’t benefiting from it. We definitely need to make changes to get that money out the door.”

The federal program also has what is known as a maintenance of effort (MOE) requirement. It says that states must [maintain a certain level](#) of state TANF spending which is based on a state’s spending for AFDC and similar programs before TANF was enacted. In other words, we needed to and did spend our taxpayer dollars on this program while we left the federal money on the table.

Worse, a good chunk of the federal dollars we did spend were spent in a questionable place—at least in relation to the purpose of the TANF program. The [Center on Budget and Policy Priorities](#) stated that nearly \$32 million of TANF money was spent on the University of Hawaii. Perhaps the justification was that the dollars went to financial aid for needy students. But CBPP pointed out that this “funding served families with incomes up to 300 percent of the federal poverty line and was not focused on helping TANF cash assistance recipients prepare for work. In comparison, the TANF benefit level for a single-parent family of three in Hawaii represents 31 percent of the federal poverty line.”

Not only that. Another central principle behind the TANF program was that states could spend more of the funds on child care subsidies — which are essential to enabling low-income parents to work — rather than on direct financial assistance. Nationally, states spent about 16% of TANF money on child care. [Hawaii spent just 5%](#).

So here we have a double-edged problem. We aren’t spending the federal money we can get, thereby increasing the burden on local taxpayers. We are spending the money on programs targeted not just to the poor, and we are as a result shortchanging the effort to get people off the dole and into the workforce. To put it another way, the money intended to help the poor is being skimmed off to do something else.

Lawmakers, wake up and smell the plumerias! Let’s get some of this federal money pulled down. Let’s get our state money directed to where it is supposed to do the most good. Maybe we can even use it to combat our homeless crisis!



LATE

To: Senator Dela Cruz, Chair
Senator Keith-Agaran, Vice Chair
Senate Committee on Ways and Means

Re: **SB 2283, Establishing a child care expense refundable tax credit**
Hawaii State Capitol, Room 211
11:00AM, 2/13/2020

Chair Dela Cruz, Vice Chair Keith-Agaran, and committee members,

On behalf of Hawaii Children's Action Network Speaks!, we offer comments of SB 2283- Relating to taxation.

Hawaii has one of the highest cost in the nation for child care. Families spend on average 14% of their income on child care, with the cost of infant care being the most expensive. We appreciate the intent of SB2283 and suggest that instead of creating a new tax credit for child care, amend the current child and dependent care tax credit so more families can access the credit and can claim more of their expenses. The existing child and dependent care tax credit is refundable and is scaled based on the tax filer's income.

The current Child and Dependent Care tax credit was the second most commonly claimed credit for year 2017 (most recent year data is available). Tax filers are familiar with and already using the child and dependent care tax credit and it seems to serve the same purpose. If the preferred method of delivery a credit for child care is through the creation of a new tax credit, we ask that the credit reflect the true costs of care, which averages \$14,000 a year in Hawaii for an infant.

We appreciate the intent of SB 2283 and the opportunity to provide comments.

Thank you,

Kathleen Algire
Director, Public Policy and Research