CHILD CARE

EMPLOYER CHILD CARE TAX CREDITS ARE INEFFECTIVE AT ALL LEVELS

Affordable, high-quality child care is fundamental for working families—but it is out of reach for far too many. In considering tax strategies to help families meet the high costs of care, policymakers have recently shown renewed interest in expanding tax credits that incentivize businesses to invest in child care for their employees. However, research demonstrates that, at both the federal and state level, such tax credits are underutilized. In fact, over time, numerous states that have enacted employer tax credits have abandoned them. Rather than pursing these failed policies, policymakers should instead invest in strategies proven to meet the child care needs of working families.

Background

It can be challenging and costly for employers to help their employees access affordable, high-quality child care. This is especially true for small businesses, where almost half of workers are employed.[1] Lawmakers in turn have attempted to encourage employers to provide child care benefits to their employees through the federal and state tax codes. Businesses that provide child care benefits to their employees may deduct the cost of doing so as a business-related expense under the federal tax code.[2] In addition, since 1981, twenty-nine states have enacted tax credits for employers who provide child care benefits,[3] and Congress enacted the federal tax credit for employer-provided child care in 2001.[4]

These tax credits allow employers who incur expenses to provide child care benefits to their employees— to reduce the amount they owe in state or federal taxes by a percentage of those expenses. For example, by building or operating an onsite child care facility, purchasing child care services from a third party, or providing resource and referral services to help employees find child care nearby.[5] The federal and different state credits vary in the kinds of expenses that can be claimed, the amount of expenses allowed, the percentage of expenses used to calculate the credit, the value of the credit (and, in some cases, the aggregate claims of the credit a state will grant, in total).[6]

The available evidence indicates that, at both the state and federal levels, these credits have not proven effective in encouraging employers to make high-quality child care more available or affordable to families.

Research has shown that state tax credits for employers providing child care benefits are underutilized and are on the decline.

- In 2002, the National Women's Law Center wrote *The Little Engine That Hasn't*, a report that analyzed state employer tax credits. At that time, 24 states had tax credits for employers providing child care benefits to employees (although one was not yet in effect),[7] and *the evidence cast significant doubt on their effectiveness.*
    - The report showed that these credits were vastly underutilized, finding that in 16 of the 20 states with employer tax credits and utilization data, *five or fewer employers* claimed the credit in the most recent tax year for which data were available.[8]
    - Between 1981 and 2002, four states had already repealed their previously enacted employer tax credits or had allowed them to expire.[9]

- Since 2002, *even fewer states offer tax credits.*
    - While 24 states had tax credits for employers providing child care benefits in 2002, only 16 states do currently.[10] Twenty-one states still have never enacted an employer child care tax credit.[11]
    - Between 2002 and 2017, nine states repealed or discontinued their tax credits for employers and businesses that provide child care benefits.[12] Another four repealed one or more of their employer tax credits or allowed them to expire, but maintained at least one other such tax credit.[13] In 2017, four states introduced legislation to repeal their tax credits.[14]
    - Only one new state has enacted a tax credit for employers providing child care benefits since 2002.[15]

The federal tax credit for employers providing child care benefits is significantly underutilized.

- *The federal tax credit for employer-provided child care has performed far below expectations.* In 2001, the Joint Committee on Taxation (JCT) estimated that employers would claim a total of $1.4 billion in the credit from 2001 to 2011, in the first 11 years of enactment.[16] Instead, employers claimed about 12 percent of that amount ($168 million total) in the first 11 years of enactment.[17] In 2013, the most recent year for which we have data, employers claimed merely $16.8 million under the federal tax credit.[18]

- *One reason that claims of the credit are low may be that many employers lack federal tax liability.* First, a few types of employers — those who are government agencies and non-profit organizations (which do not have tax liability) — are not eligible to claim the credit.[19] Second, of the corporate employers who are eligible to claim the credit, many actually lack tax liability against which this nonrefundable credit may be applied. A recent GAO study concluded that, "[i]n each year from 2006-2012, at least two-thirds of all active U.S. corporations had no federal income tax liability."[20] And now that corporate tax rates have been lowered,[21] even fewer corporations may have federal tax liability. In the absence of tax liability, the nonrefundable Employer-Provided Child Care Credit has no value to an employer.

The evidence is clear: incentivizing employers to invest in child care through tax credits is an ineffective strategy.

Instead of pushing to further expand this failed tax strategy, policymakers should be investing in child care initiatives proven to work, such as:

- *Increasing investments at the federal and state levels in the Child Care and Development Block Grant (CCDBG);*
- *Improving the federal Child and Dependent Care Tax Credit (CDCTC); and*
- *Enacting or improving state Child and Dependent Care (CADC) tax provisions.*

[1] U.S. Small Business Admin., Office of Advocacy, Small Business Profile 2016 (Mar. 9, 2016), *available at* https://www.sba.gov/sites/default/files/advocacy/United_States.pdf.

[2] 26 U.S.C. § 162 (2018).

[3] Since 1981, 29 states have enacted one or more tax credits for employers providing child care benefits: Arizona, Arkansas, California, Colorado, Connecticut, Florida, Georgia, Illinois, Kansas, Louisiana, Maine, Maryland, Michigan, Mississippi, Montana, Nebraska, Nevada, New Jersey, New Mexico, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Texas, Virginia, and Wisconsin. *See* Ariz. Rev. Stat. Ann. §§ 43-1075(A), -1163(A) (1994) (sunsetting in 2015); Ark. Code Ann. §§ 26-51-507 to -508, -52-516, -53-132 (2017); Cal. Rev. & Tax Code §§ 17052.17–.18, 23617 (Deering 2005), *repealed by* 2006 Cal. Stat. Ch. 712, §§ 1–2; Colo. Rev. Stat. §§ 39-22-121, -517, -521 (2017); Conn. Gen. Stat. §§ 12-217x, -634 (2017); Fla. Stat. §§ 220.19, 624.5107 (2008), *amended by* 2009 Fla. Laws ch. 2009-20, §§ 5, 19; Fla. Stat. § 411.0102 (2012), *repealed by* 2013 Fla. Laws ch. 252, § 29; Ga. Code Ann. § 48-7-40.6 (2017); 35 Ill. Comp. Stat. 5/210 (2017); Kan. Stat. Ann. § 79-32,190 (2017); La. Stat. Ann. § 47:6107 (2017); 36 Me. Rev. Stat. § 2524 (2014), *amended by* 2015 Me. Laws ch. 390, § 6; 36 Me. Rev. Stat. § 5217 (2014), *amended by* 2015 Me. Laws ch. 267, § DD-22; Md. Code Ann., Educ. § 21-309 (2017); Md. Code Ann., Ins. § 6-115 (2017); Md. Code Ann., Tax – Gen. §§ 8-413, 8-216 (2017); Md. Code Ann., Tax – Gen. § 8-410 (2007), *repealed by* 2008 Md. Laws, ch. 391, § 1; Md. Code Ann., Ins. § 6-105.1 (2006), *repealed by* 2007 Md. Laws, ch. 370, § 4; Md. Code Ann., Tax – Gen. § 8-213 (2006), *repealed by* 2007 Md. Laws, ch. 370, § 2; Mich. Comp. Laws § 208.39a(b)(4) (1991), *repealed by* 1993 Mich. Pub. Acts, no. 329, § 2; Miss. Code Ann. § 57-73-23 (2017); Mont. Code Ann. §§ 15-30-2373, -31-131, -31-133 (2017); Neb. Rev. Stat. § 77-27,222 (2006), *repealed by* 2007 Neb. Laws ch. 367, § 30; Nev. Rev. Stat. § 364A.140 (2002), *repealed by* 2003 Nev. Stat. ch. 5, § 186; 1999 N.J. Laws, ch. 102; 1999 N.J. Laws, ch. 108; N.M. Stat. Ann. § 7-2A-14 (2017); Ohio Rev. Code Ann. §§ 5733.36–38 (2017); Ohio Rev. Code Ann. §§ 5747.34–.36 (2014), *repealed by* 2015 Ohio Laws, File 30, § 2; Okl. St. tit. 68, § 2357.26 (2012), *repealed by* 2013 Okla. Sess. Laws ch. 363, § 7; Or. Rev. Stat. §§ 315.204, .208, .213 (2017); Or. Rev. Stat. §§ 329A.703, .706 (2017); 72 Pa. Stat. Ann. §§ 8703-A, 8706-A (2003), *amended by* 2004 Pa. Laws 116; R.I. Gen. Laws §§ 44-47-1, -3 (2017); S.c. Code Ann. § 12-6-3440 (2017); Tenn. Code Ann. § 67-4-2009(3) (2008), *repealed by* 2009 Tenn. Pub. Acts, ch. 530, §2; Tex. Tax Code Ann. §§ 171.701 – 171.707 (2005), *repealed by* 2006 Tex. Gen. Laws 79th Leg. 3rd C.S., ch. 1, §18(a)(3); Va. Code Ann. § 58.1-439.4 (2017); Wis. Stat. § 71.07(2dd) (1996), *repealed by* 1997 Wis. Sess. Laws, Act 27, § 2261h.

[4] 26 U.S.C. § 45F (2018).

[5] Christina Smith Fitzpatrick & Nancy Duff Campbell, Nat'l Women's Law Ctr., The Little Engine That Hasn't: The Poor Performance Of Employer Tax Credits For Child Care 15 (2002), *available at* https://nwlc.org/wp-content/uploads/2015/08/TheLittleEngine2002.pdf.

[6] *See generally* Fitzpatrick & Campbell, *supra* note 5; 26 U.S.C. § 45F (2018).

[7] In 2002, the following 24 states had one or more employer tax credits: Arkansas, California, Colorado, Connecticut, Florida, Georgia, Illinois, Kansas, Maine, Maryland, Mississippi, Montana, Nebraska, Nevada, New Mexico, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Texas, and Virginia. *See*, Fitzpatrick & Campbell, *supra* note 5, at 49-50.

[8] Fitzpatrick & Campbell, *supra* note 5, at 5. *See also id.* at 31–32 (finding that in the 17 states with employer child care tax credits and tax liability data, on average, 57 percent of state corporate filers had no tax liability and 93 percent of state corporate filers did not have sufficient tax liability to take advantage of the full amount of the credit for which they were eligible).

[9] In the years leading up to the 2002 report, four states repealed their tax credits for employers providing child care benefits or allowed them to sunset: Michigan (1982), Arizona (1995), Wisconsin (1997), and New Jersey (2001). *See* Mich. Comp. Laws § 208.39a(b)(4) (1991), *repealed by* 1993 Mich. Pub. Acts, no. 329, § 2 (showing the Michigan credit sunset in 1983 and was repealed effective in 1994); Ariz. Rev. Stat. Ann. § 43-1075(A) (1994) (showing the sunset date for the credit); Ariz. Rev. Stat. Ann. § 43-1163(A) (1994) (showing the sunset date for the credit); 1997 Wis. Sess. Laws, Act 27, § 2261h; 1999 N.J. Laws, ch. 102, § 3 (establishing a sunset date for the Neighborhood and Business Child Care Tax Incentive Program); 1999 N.J. Laws, ch. 108, § 9 (establishing a sunset date for the Small-Medium Business Child Care Consortium Incentive Demonstration Program).

[10] The 16 states that currently have tax credits for employers or businesses providing child care benefits are Arkansas, Colorado, Connecticut, Georgia, Illinois, Kansas, Louisiana, Maryland, Mississippi, Montana, New Mexico, Ohio, Oregon, Rhode Island, South Carolina, and Virginia. *See* Ark. Code Ann. §§ 26-51-507 to -508, -52-516, -53-132 (2017); Colo. Rev. Stat. §§ 39-22-121, -517, -521 (2017); Conn. Gen. Stat. §§ 12-217X, -634 (2017); Ga. Code Ann. § 48-7-40.6 (2017); 35 Ill. Comp. Stat. 5/210 (2017); Kan. Stat. Ann. § 79-32,190 (2017); La. Stat. Ann. § 47:6107 (2017); Md. Code Ann., Educ. § 21-309 (2017); Md. Code Ann., Ins. § 6-115 (2017); Md. Code Ann., Tax – Gen. §§ 8-413, 8-216 (2017); Miss. Code Ann. § 57-73-23 (2017); Mont. Code Ann. §§ 15-30-2373, -31-131, -31-133 (2017); N.m. Stat. Ann. § 7-2A-14 (2017); Ohio Rev. Code Ann. § 5709.65 (2017); Or. Rev. Stat. §§ 315.204, .208, .213 (2017); Or. Rev. Stat. §§ 329A.703, .706 (2017); R.i. Gen. Laws §§ 44-47-1, -3 (2017); S.c. Code Ann. § 12-6-3440 (2017); Va. Code Ann. § 58.1-439.4 (2017).

[11] The twenty-one states that have never enacted a tax credit for employers providing child care benefits are Alabama, Alaska, Delaware, Hawaii, Idaho, Indiana, Iowa, Kentucky, Massachusetts, Minnesota, Missouri, New Hampshire, New York, North Carolina, North Dakota, South Dakota, Utah, Vermont, Washington, West Virginia, and Wyoming.

[12] The nine states that have repealed or discontinued all of their tax credits for employers providing child care benefits since 2002 (and the years in which the states repealed their tax credits) are Nevada (2003), Nebraska (2007), Texas (2008), Florida (2009), Pennsylvania (2009), Tennessee (2009), California (2012), Oklahoma (2014), and Maine (2015). *See* 2003 Nev. Stat. ch. 5, § 186; 2007 Neb. Laws ch. 367, § 30; 2006 Tex. Gen. Laws 79th Leg. 3rd C.S., ch. 1, §18(a)(3); 2009 Fla. Laws ch. 2009-20, §§ 5, 19; 2013 Fla. Laws ch. 252, § 29; 2004 Pa. Laws 116; 2009 Tenn. Pub. Acts, ch. 530, §2; 2006 Cal. Stat. ch. 712, §§ 1-2; 2013 Okla. Sess. Laws ch. 363, § 7; 2015 Me. Laws ch. 390, § 6.

[13] Since 2002, four states have repealed or discontinued one or more tax credits while keeping at least one other tax credit for employers providing child care benefits: Maryland, Montana, Ohio, and Oregon. *Compare* Md. Code Ann., Educ. § 21-309 (2017), Md. Code Ann., Ins. § 6-115 (2017), Md. Code Ann., Tax – Gen. §§ 8-413, 8-216 (2017), Mont. Code Ann. §§ 15-30-2373, -31-131 (2017), Ohio Rev. Code Ann. §§ 5733.36–38 (2017), Or. Rev. Stat. §§ 315.204, .213 (2017), *and* Or. Rev. Stat. §§ 329A.703, .706 (2017), *with* Md. Code Ann., Tax – Gen. § 8-410 (2007), *repealed by* 2008 Md. Laws, ch. 391, § 1, Md. Code Ann., Ins. § 6-105.1 (2006), *repealed by* 2007 Md. Laws, ch. 370, § 4, Md. Code Ann., Tax – Gen. § 8-213 (2006), *repealed by* 2007 Md. Laws, ch. 370, § 2, Mont. Code Ann. §§ 15-31-133 (2017) (credit only applies to facilities built before 2006), Ohio Rev. Code Ann. §§ 5747.34–.36 (2014), *repealed by* 2015 Ohio Laws, File 30, § 2, *and* Or. Rev. Stat. § 315.208 (2017) (credit only applies to facilities built before 2002). Three states introduced, but did not pass, legislation in 2017 to revive a repealed or expired tax credit: Florida, Maine, and Nevada. *See* H.B. 1329, 2017 Leg, 1st Reg. Sess. (Fla. 2017); H.P. 914, 128th Leg., 1st Reg. Sess. (Me. 2017); S.B. 147, 79th Leg.,

Reg. Sess. (Nev. 2017); S.B. 455, 79th Leg., Reg. Sess. (Nev. 2017).

14 The four states that introduced, but did not pass, legislation in 2017 to repeal their tax credits for employers providing child care benefits were Kansas, Louisiana, New Mexico, and Virginia. *See* H.B. 2432, 2017 Leg., 1st Sess. (Kan. 2017); H.B. 2237, 2017 Leg., 1st Sess. (Kan. 2017); S.B. 186, 43d Leg., Reg. Sess. (La. 2017); S.B. 123, 53d Leg., 1st Sess. (N.M. 2017); S.B. 460, 53d Leg., 1st Sess. (N.M. 2017); S.B. 1485, 2017 Leg., 1st Sess. (Va. 2017).

15 Louisiana enacted a tax credit for business-supported child care in 2007, which went into effect in 2008. La. Rev. Stat. Ann. § 47:6107(A) (2017). There is a separate credit for businesses that make donations to child care resource and referral agencies. La. Rev. Stat. Ann. § 47:6107(B) (2017).

16 Joint Comm. on Tax'n, JCX-51-01, Estimated Budget Effects Of The Conference Agreement For H.R. 1836, at 7 (2001), *available at* https://www.jct.gov/publications.html?func=startdown&id=2001.

17 NWLC calculations based on Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2002, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $11.7 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2003, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $13.9 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2004, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $14.5 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2005, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $14 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2006, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $15.1 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2007, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $15.9 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2008, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $15.2 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2009, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $15.2 million); Internal Revenue Serv., SOITax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2010, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $15.4 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2011, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $15.3 million); Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2012, *available at* https://www.irs.gov/uac/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s (showing claims of $17.18 million).

18 Internal Revenue Serv., SOI Tax Stats – Table 21 – Returns Of Active Corporations, Tax Year 2013, *available at* https://www.irs.gov/statistics/soi-tax-stats-table-21-returns-of-active-corporations-other-than-forms-1120-reit-1120-ric-and-1120s.

19 *See* 26 U.S.C. § 115 (2018) (exempting government entities from taxation); *see, e.g., id*. § 501(a) (exempting charitable organizations described in § 501 from taxation).

20 U.S. Gov't Accountability Office, GAO-16-363, Corporate Income Tax: Most Large Profitable U.S. Corporations Paid Tax but Effective Tax Rates Differed Slightly from the Statutory Rate 10 (2016), *available at* https://www.gao.gov/assets/680/675844.pdf. The GAO analyzed "active corporations filing tax forms 1120 (U.S. Corporation Income Tax Return), 1120-L (U.S. Life Insurance Company Income Tax Return), 1120-PC (U.S. Property and Casualty Insurance Company Income Tax Return), and 1120-F (U.S. Income Tax Return of a Foreign Corporation)," as well as large corporations that filed Schedules M-3, and thus the data do not include "certain 'pass-through' entities," *id.* at 2 n.3, or non-profits and government agencies.

21 Tax Cuts and Jobs Act, Pub. L. No. 115-97 § 13001, 131 Stat 2054, 2096 (2017).