

**TESTIMONY OF  
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DEPARTMENT OF ADMINISTRATIVE AND FINANCIAL SERVICES**

Before the Joint Standing Committee on Taxation  
Hearing Date: *April 11, 2023*

*LD 1222 – “An Act to Expand Child Care Services Through an Employer-supported Tax Credit”*

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Senator Grohoski, Representative Perry, and members of the Taxation Committee – good afternoon, my name is Michael Allen, Associate Commissioner for Tax Policy in the Department of Administrative and Financial Services. I am testifying at the request of the Administration Against LD 1222, *“An Act to Expand Child Care Services Through an Employer-supported Tax Credit.”*

Expanding access to child care has been, and continues to be, an important goal of the Administration. Parents need high quality affordable child care in order to go to work and kids need a safe place to learn and grow during the day. Towards that goal, the Administration has invested over a \$100 million to increase access to high-quality care and support for Maine’s child care workforce in line with the Office of Child and Family Services’ Child Care Plan for Maine. In addition, the Governor’s biennial budget proposed investing approximately \$240 million to strengthen Maine’s education and early care system and provide critical supports to children, youth and their families.

In addition to non-tax programs, the State currently provides child care benefits through conformity to the federal tax treatment of dependent care Flexible Spending Accounts or FSAs, and through the child care tax credit. While the Administration supports the goals of the bill, those goals can be better addressed without creating another child care income tax benefit.

For tax years beginning on or after January 1, 2024, the bill creates the refundable employer-supported quality child care credit for employers that provide child care services for children of its employees. Providing child care services means (1) expenses, or in-kind resources, used to build, furnish, license, staff, operate, or subsidize a child care center licensed by the Maine DHHS to provide early care and education services to the children of employees at no profit to the employer, or to contract with a child care facility licensed by, or registered with, the DHHS to provide early care and education services to the children of employees; (2) payments made to employees to pay for early care and education services under a dependent care assistance program (also known as a dependent care Flexible Spending Account or FSA); and (3) the provision of child care resources and referral services to employees. The credit, available for individual, fiduciary, and corporate income tax taxpayers, is equal to the lower of 50% of the cost of providing child care services or \$3,000 for each child of an employee for which the employer is providing child care services.

The benefit of this credit will primarily accrue to large business that can navigate the complexities of both this credit and the provision of dependent care benefits. For instance, businesses that can administer a dependent care FSA and provide an employer contribution.

Dependent care FSAs already receive significant tax benefits at the federal and State level. Employers receive an income tax deduction for their contributions and the resulting income is excluded from the employee's income. In addition, contributions are exempt from both the employer and employee portion of FICA (Social Security and Medicare) taxes. Careful consideration should be given before allowing additional tax benefits to FSA contributions.

The bill also repeals the employer-assisted day care credit. Except for the carryover of unused credit amounts, the nonrefundable employer-assisted day care credit could be claimed for tax years beginning on or after January 1, 1988 and before January 1, 2016 and applied against individual, fiduciary, and corporate income taxes and the insurance premiums tax. The credit was limited to the lower of \$5,000, 20% of the costs incurred to provide day care services for children of employees, or \$100.00 for each child of an employee enrolled in day care services. For tax years beginning after 2000, the credit amount was doubled if the day care services provided was for quality child care services, as defined by 36 M.R.S. § 5219-Q. Unused portions of the credit could be carried forward for up to 15 years or carried back for three years. The credit was sunset as part of the 2016-2017 biennial budget due to lack of use and for tax simplification.

The State's experience with the employer-assisted day care credit should be taken into account when considering this new proposal. While the credit targeted an important need of the State, additional child care, the attempt to address the issue through the tax code was ultimately unsuccessful, resulting in few, if any, employers taking the credit. At the same time, it added additional complexity to an already complex State income tax code.

The Administration also notes the following technical concerns:

- The bill does not provide an application date for the repealed credit.
- The bill does not repeal the employer-assisted day care credit for, nor does it extend the proposed credit to, employers subject to insurance premiums tax under 36 M.R.S., Part 4, Chapter 357.

- If the bill is intended to coordinate with specific programs administered by DHHS, such as the Help Me Grow Maine Program, the First4ME Program, or the Rising Stars for ME Program to be eligible for the credit, and or a rating system such as the Quality for ME Program or the Quality Rating and Improvement System (QRIS), that coordination should be clarified.
- The bill should define “dependent care assistance program” or cite the IRC if it is intended to refer to dependent care FSAs.
- The bill should clarify whether “children of the employee” includes stepchildren and grandchildren, etc.
- The bill should clarify its application to nonprofit and local government entities that do not normally file income tax returns or receive income tax credits.
- The carry-over provision is unnecessary because the credit is refundable.
- For purposes of evaluation of the credit, the bill does not detail the public policy objective or provide performance measures by which to determine whether the policy objectives have been achieved.
- The bill will provide an additional benefit for employers that have claimed the cost of providing child care as an ordinary and necessary business expense under IRC Section 162(a).

The estimated revenue impact of the bill is a revenue loss of approximately \$5 million per year.

The estimated administrative costs are \$33,000 in fiscal year 2025 for one-time computer programming costs to add an additional line to the individual, fiduciary, and corporate income tax returns to accommodate the credit, update

check stub messages and notices, make federal tape changes, and perform system testing.

The Administration looks forward to working with the Committee on the bill; representatives from MRS will be here for the Work Session to provide additional information and respond in detail to the Committee's questions.