Legislative Analysis

CHILD CARE SAVINGS PROGRAM

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House Bills 4056 and 4057 as introduced
Sponsor: Rep. Bill G. Schuette
Committee: Economic Competitiveness
Complete to 3-20-25

SUMMARY:

House Bills 4056 and 4057 together would create the child care savings program, which would allow individuals to create a savings account with state individual income tax benefits for the purpose of paying for child care expenses.

House Bill 4056 would create a new act, the Child Care Savings Program Act, to establish the child care savings program in the Department of Treasury. The purposes, powers, and duties of the program would be vested in and exercised by the state treasurer or their designee.

Under the act, beginning January 1, 2026, an individual could open an account with a ***financial institution*** and designate that account, in its entirety, as a ***child care savings account*** to be used to pay for or reimburse ***eligible costs*** for child care.

> ***Financial institution*** would mean a bank, trust company, savings institution, industrial loan association, consumer finance company, credit union, or a benefit association, insurance company, safe deposit company, money market mutual fund, broker, or similar entity authorized to do business in Michigan.
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> ***Child care savings account*** would mean an account with a financial institution that an account holder designates as a child care savings account on their income tax return under the act, for the purpose of paying or reimbursing eligible costs.
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> ***Eligible costs*** would mean costs incurred for the care and supervision of a ***qualified individual*** that are necessary for the account holder to be employed, attend educational or vocational training programs, improve employment opportunities, or search for employment.
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> Generally speaking, ***qualified individual*** would mean a child or other dependent of the account holder who is younger than 14 years of age on the last day of the tax year.

An individual could jointly hold a child care savings account with another person if the joint account holders file a joint return under the Income Tax Act. An individual could be the account holder of more than one account, and an individual could open an account in anticipation of having a qualified individual for whom they may incur eligible costs without having to designate a qualified individual at the time they open the account.

Contributions and withdrawals

Only cash and marketable securities could be contributed to a child care savings account, and anyone could contribute. Contributions to an account, interest earned on those contributions, and ***qualified withdrawals*** from the account would be exempt from taxation.[1]

> ***Qualified withdrawal*** would mean a withdrawal from an account that meets all of the following:
> - It is not subject to a penalty under the act.
> - It is not subject to taxation under the Income Tax Act.
> - It is used to pay the eligible costs of an account holder incurred after the account is established.

If funds are withdrawn from an account for any purpose other than the payment or reimbursement of eligible costs by the account holder, a 10% penalty payable to the Department of Treasury would be assessed on the amount withdrawn. The penalty would not apply if the funds withdrawn are any of the following:

- Withdrawn because of the account holder's or qualified individual's death.
- A disbursement of assets of the account pursuant to a filing for protection under chapter 11 of the United States Bankruptcy Code.
- Transferred from one child care savings account into another.
- Withdrawn because of a hardship withdrawal as described below.

The account holder would be responsible for the use or application of funds in the account. The account holder could not use the funds in an account to pay expenses of administering the account, except that the financial institution could deduct a service fee from the account. An account holder could withdraw funds from an account and deposit them in a new account held by the same or a different financial institution.

If necessary, an account holder could make a hardship withdrawal from the account due to an immediate and heavy financial need of the account holder. However, the amount withdrawn would have to be limited to what is needed to meet that need. A hardship withdrawal would not be a qualified withdrawal and would be subject to taxation under the Income Tax Act.

Documentation, forms, and rules

An account holder would have to submit all of the following to the Department of Treasury, in addition to the form described below, with their state income tax return:

- Account statements that show the contributions during the tax year and the taxable interest or earnings on the account for the applicable tax year.
- The applicable Form 1099 issued by the financial institution for the account.
- Upon withdrawal of funds, a copy of a detailed receipt indicating that the withdrawal was used for eligible costs.

An account holder would have to maintain and keep suitable records and documentation for each account for at least four years, including account statements for all contributions and withdrawals made, a detailed list describing account transactions, and other records and papers as required by the Department of Treasury.

[1] Subject to limitations contained in House Bill 4057, as described below.

The Department of Treasury would have to prescribe the form and manner for claiming the income tax deduction in accordance with the act and the Income Tax Act (as would be provided for in HB 4057). The form would have to include the names of the account holder and each qualified individual for whom eligible child care expenses were incurred, the name of the financial institution and the account number for the account, the beginning and end of year account balance, and the amount of the deduction claimed.

The state treasurer could promulgate rules to implement the program. The rules could not apply to financial institutions-related accounts for child care savings accounts or impose administrative, reporting, or other obligations or requirements on those accounts. The Department of Treasury also could prepare and distribute informational materials about the program to financial institutions to publicize its availability.

Financial institutions

A financial institution would not be required to do any of the following:

- Designate an account as a child care savings account in its contracts or systems (or in any other way).
- Track the use of money withdrawn from an account.
- Allocate funds in account among joint account holders.
- Report any information to the Department of Treasury that is not otherwise required by law.

A financial institution would not be responsible or liable for any of the following:

- Determining or ensuring that an account satisfies the requirements to be a child care savings account.
- Determining or ensuring that funds in an account are used for eligible costs.
- Reporting or remitting taxes or penalties related to the use of an account.

If provided with proof of the death of the account holder and any other information required by the savings account contract, a financial institution would have to distribute the principal and accumulated interest in the account in accordance with the terms of the contract.

House Bill 4057 would amend the Income Tax Act to provide for the individual income tax benefits of the child care savings program accounts as follows:

For tax years that begin on and after January 1, 2026, a taxpayer could deduct all of the following:

- To the extent not deducted in determining adjusted gross income (AGI), the difference between contributions to and qualified withdrawals from a child care savings account, up to a total deduction of $10,000 for a single return or $20,000 for a joint return per tax year. The amount calculated could not be less than zero.
- To the extent not deducted in determining AGI, interest earned in the tax year on the contributions to the account.
- To the extent included in AGI, distributions that are qualified withdrawals from a child care savings account.

For tax years that begin on and after January 1, 2026, the taxpayer would add, to the extent not included in AGI, the amount of withdrawals by the taxpayer in the tax year from the account that are not qualified withdrawals (as defined by HB 4056), not to exceed the total amount deducted under the above provisions in that tax year and all previous tax years. (This provision would not apply to withdrawals that are less than the sum of all contributions made to an account in all previous tax years for which no deduction was claimed, less any contributions for which no deduction was claimed that were withdrawn in all previous tax years.)

MCL 206.30

The bills are tie-barred together, which means that neither one can take effect unless both are enacted.

FISCAL IMPACT:

The bills would reduce income tax revenue by an unknown amount. The two main factors in estimating a revenue loss impact, the number of participants and the amount participants would contribute to child care savings accounts, cannot be determined with any accuracy.

There are two federal child care benefit programs, the employer-sponsored dependent care flexible spending account and the child and dependent care tax credit, that offer better tax benefits that would likely mitigate participation in the child care savings account under the bill thereby limiting the overall fiscal impact. The contribution caps under the proposed child care savings program exceed the contribution or expense limits under both federal programs and may serve to augment the existing federal benefits.

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