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Supporting Michigan's Working Families:
Opportunities through Child Care Tax Credits

Families need affordable, high quality child care that supports their children's learning and development while parents work or engage in job training. Access to high quality child care can ensure that young children are building the foundation they need to learn soft skills, develop basic literacy, and protect against poverty-related risk factors while reducing the equity gap. For school-aged children, access to high quality after-school programming can provide academic and other supports outside of the school day to engage them in learning, build new skills and help them stay academically on-track. The research is clear that high quality child care provides the greatest benefit to the state's most challenged children and youth, including children of color and children from low-income families.

Tax credits connected to child care can be a valuable tool to provide financial incentives to encourage more child care providers to increase the quality of their programs and for parents to choose higher quality – and subsequently more expensive – care. Tax credits are direct dollar-for-dollar reductions in the tax liabilities owed by taxpayers. Refundable tax credits allow taxpayers to receive a check for the amount of the credit if they have no tax obligation, which is particularly important for nonprofit child care providers and for low-income families.

Tax credits can be a particularly effective strategy since they are built into an already existing and familiar system that state collection agencies can administer. Additionally, tax credits do not carry the same stigma that other public assistance programs may have for families who face financial challenges. Furthermore, tax credits are relatively stable and not a part of the annual state appropriation budgeting process that places many public service programs at risk for disinvestment each year.

The Louisiana Model

Louisiana's system, known as the School Readiness Tax Credits (SRTC), is the country's most innovative and far-reaching state effort to use tax credits to promote high quality early childhood education. The Louisiana model is particularly successful since the strategy focuses on building capacity in the child care system itself. Specifically, the SRTC builds upon the state's efforts to: move more providers into the state's Quality Rating and Improvement System (QRIS); incentivize more parents to opt-into higher rated care; provide more means for child care teachers and directors to grow professionally; and for businesses to financially support the child care system. By providing tax credits that are financially rewarding, Louisiana has successfully moved their entire child care system to higher levels of quality.

Louisiana's SRTC is a package of four tax credits aimed to increase the quality of and access to child care.

1. Families: Tax credits are provided to families with children enrolled in a child care program that has a rating in the state's Quality Rating and Improvement System (QRIS) of at least two out of a total of five stars. The tax credit increases in value as families access higher-rated child care programs, incentivizing families to opt for higher quality care. The credit is refundable for families whose adjusted gross income is $25,000 or less. Families making more than $25,000 may apply the credit to their tax liability; and if the credit is more than their liability, the remaining credit can be carried

forward and applied to later tax years. The total credit amount is based on Louisiana's basic child care tax credit available to all families who utilize child care. The additional SRTC ranges from 50% of the base child care tax credit for families who opt into 2-star rated programs, 100% for 3-star rated programs, 150% for 4-star rated programs, and 200% for 5-star rated programs.

2. Child Care Programs: Child care providers who participate in the QRIS are eligible for a refundable tax credit based on the number of stars they earn and the number of children they serve who are subsidized by their state's child care subsidy system or are in foster care. This credit is available to both for-profit and not-for-profit child care programs, and range from $750 per child to $1,500 per child. Since the tax credit is refundable, it acts as an annual grant to child care programs, many of which have tight budgets that may make it difficult to maintain and/or improve the quality of their services.
3. Child Care Teachers and Directors: Teachers and directors are eligible to receive a refundable tax credit if they teach in a child care program that participates in the QRIS. The tax credit is based on the level of education the individual has attained, and ranges from $1,600 to $3,200. Because the tax credit is refundable, in an industry where wages are low, teachers and directors essentially receive a wage subsidy in the form of a tax refund.
4. Businesses: Businesses that provide financial support to child care programs that participate in the QRIS are eligible for a credit with its value based on the star rating of the child care program. Businesses can receive a credit for support used to construct, renovate, expand, or repair an eligible child care center or purchase equipment; or to support employees' child care needs either by making payments directly to a child care center or by purchasing slots at a child care center. Based on these expenses, businesses receive a refundable credit of 5% of the total donation for 2-star rated programs, 10% for 3-star, 15% for 4-star, and 20% for 5-star rated programs. Businesses may also receive a tax credit for donations up to $5,000 made to child care resource and referral agencies.

Opportunities in Michigan

Michigan is well-poised to implement a child care tax credit system similar to the Louisiana model – particularly as it relates to the credits for child care programs, families, and teachers and directors. Michigan began implementing its QRIS – Great Start to Quality – in 2010 but has struggled with participation by providers and awareness by families seeking child care. Though support through the federal Race to the Top – Early Learning Challenge grant that Michigan was awarded will focus on moving more providers through Great Start to Quality, consistent financial incentives will be needed by child care providers to maintain and support higher levels of quality. Providing additional tax credits to families tied directly to the quality of care would not only assist them financially but could also serve as an excellent marketing tool to make more families aware of Great Start to Quality and encourage more families to seek higher quality care.

Additionally, though Michigan has opportunities for child care teachers and directors to continue to obtain higher credentials through TEACH scholarships, these professionals continue to be undervalued and underpaid. A refundable credit to child care teachers and directors will allow them to support their professional development in ways that they may not otherwise be able to financially afford. And finally, providing opportunities for employers to support their employees' child care needs will ensure that businesses can stay productive while families' needs are met. Seeking a child care tax credit system similar to the Louisiana model would allow Michigan to take full advantage of the great work that has been done to institute Great Start to Quality and would raise the overall quality of the child care system to ensure that children can thrive while their parents work.