

A Working Parent's Guide to the Child and Dependent Care Tax Credit

As working parents of young children know, paying for child care can take a big bite out of the family budget. The Federal government offers a number of tax breaks, including the Child and Dependent Care Credit, designed to ease the financial burdens of working families. The amount that can be claimed varies considerably, however, based on the outlays for care, the income of the parents, and the number of children or other dependents requiring care.

If you pay a babysitter, day care center, or other provider to care for your child or a qualifying spouse or dependent so that you can go to work or look for work, you may be able to claim the Child and Dependent Care Credit on your Federal income tax return. To qualify, children must be under age 13 at the time the care is provided, while spouses or other dependents must be physically or mentally incapable of caring for themselves.

The Child and Dependent Care Credit is a percentage of the amount of work-related child and dependent care expenses paid to a care provider. Depending upon your income, the credit can be up to 35% of your qualifying expenses. You may claim up to \$3,000 of the expenses paid in one year for one dependent or \$6,000 for two or more qualifying dependents.

In practice, however, relatively few taxpayers can claim the full 35% rate: For taxpayers with annual adjusted gross incomes (AGIs) that exceed \$15,000, the credit percentage is incrementally phased down, falling to 20% for those making more than \$43,000 per year. The dollar limits on the credits that may be claimed are also reduced by the amount of any dependent care benefits provided by your employer that is excluded from your income. Moreover, the credit is not refundable, and only serves to reduce the amount of taxes owed.

If, for example, you spent \$4,000 on care for one child during the year, up to \$3,000 could be applied toward the credit. If your income is very low, you would be able to claim 35% of this amount, for a total tax credit of \$1,050. If, however, you paid \$9,000 over the course of the year for child care for three children, but your AGI is \$75,000 per year, you would be permitted to claim 20% of \$6,000 of these expenses, for a total credit of \$1,200.

There are a number of conditions that taxpayers are required to meet when claiming the credit. To qualify, you must have earned income from wages, salaries, tips, other taxable employee compensation, or net earnings from self-employment. The babysitter or other caregiver cannot be someone you can claim as your dependent on your tax return or your child who is under age 19, even if he or she is not your dependent. In addition, the dependent for whom the care is provided must have

lived with you for more than half the year. Finally, if you are married, you cannot claim the credit when filing separately.

Families in which one of the spouses is a full-time homemaker and does not earn income outside the home generally are not eligible to claim the Child and Dependent Care Credit. If you are married and paid someone to care for a child or other qualifying individual, both you and your spouse must have earned income to claim the credit, unless one spouse is either a full-time student or is physically or mentally incapable of self-care.

The Federal government does, however, allow you to include payments to a wide range of care providers when claiming the credit. These include licensed day care centers, after-school care, day camps (but not overnight camps), nurseries or pre-schools (with school costs separated from child care costs), and household services, provided the assistance is necessary for the protection and well-being of the dependent. Keep in mind that additional employment taxes may be due if you hire someone, such as a nanny or housekeeper, to come to your home to care for your children or other dependents.

When claiming the credit on your tax return, you must report the name, address, and taxpayer identification number of the care provider. For individual caregivers, this is the Social Security number. If the care provider is tax exempt, only the name and address must be reported on your return. If you are unable to provide information regarding the care provider, you may still be eligible for the credit if you can demonstrate that you exercised due diligence in attempting to obtain the required information.

For more information on the Child and Dependent Care Tax Credit, talk to your tax professional.

TXCHILDC-X