School’s Out - Who Is Going to Take Care of the Kids?

Article Highlights:

- Child Age Limits
- Employment-Related Expense
- Married Taxpayer Earnings Limits
- Disabled or Full-Time-Student Spouse
- Expense Limits

Summer has just arrived, and there is a tax break that working parents should know about. Many working parents must arrange for care of their children under 13 years of age (or any age if handicapped) during the school vacation period. A popular solution — with a tax benefit — is a day camp program. The cost of day camp can count as an expense toward the child and dependent care credit. But be careful; expenses for overnight camps do not qualify.

For an expense to qualify for the credit, it must be an “employment-related” expense; i.e., it must enable you and your spouse, if married, to work, and it must be for the care of your child, stepchild, foster child, brother, sister or stepsibling (or a descendant of any of these) who is under 13, lives in your home for more than half the year and does not provide more than half of his or her own support for the year. Married couples must file jointly, and both spouses must work (or one spouse must be a full-time student or disabled) to claim the credit.

The qualifying expenses are limited to the income you or your spouse, if married, earn from work, using the figure for whoever earns less. However, under certain conditions, when one spouse has no actual earned income and that spouse is a full-time student or disabled, that spouse is considered to have a monthly income of $250 (if the couple has one qualifying child) or $500 (two or more qualifying children). This means the income limitation is essentially removed for a spouse who is a student or disabled.

The qualifying expenses can’t exceed $3,000 per year if you have one qualifying child, while the limit is $6,000 per year for two or more qualifying persons. This limit does not need to be divided equally. For example, if you paid and incurred $2,500 of qualified expenses for the care of one child and $3,500 for the care of another child, you can use the total, $6,000, to figure the credit. The credit is computed as a percentage of your qualifying expenses; in most cases, 20%. (If your joint adjusted gross income [AGI] is $43,000 or less, the percentage will be higher, but it will not exceed 35%.)

> *Example:* Al and Janice both work, each with earned income in excess of $40,000 per year. Janice has a part-time job, and her work hours coincide with the school hours of their 11-year-old daughter, Susan. However, during the summer vacation period, they place Susan in a day camp program that costs $4,000. Since the expense limitation for one child is $3,000, their child credit would be $600 (20% of $3,000).

The credit reduces a taxpayer’s tax bill dollar for dollar. Thus, in the above example, Al and Janice pay $600 less in taxes by virtue of the credit. However, the credit can only offset income tax and alternative minimum tax liability, and any excess is not refundable. The credit cannot be used to reduce self-employment tax or the taxes imposed by the Affordable Care Act.

If you have questions about how the childcare credit applies to your particular tax situation, please give this office a call.