



Dependent Daycare

There are two ways to get a tax break on your dependent daycare expenses. You can use either the income tax credit on Form 2441 of your 1040, or you can use the Section 125 Plan and *get your benefit in every paycheck*. Your tax advisor can help you decide which tax break will save the most money for your family. Here are some general guidelines which may help you:

Generally, if you are a single parent and your income is \$24,000 or less, you may be better off using the tax credit and not the Section 125 Plan. That figure goes up to \$35,000 (total) for two wage earners in the family. If your income is higher than the above, there are three reasons why you might use the Section 125 Plan and not the tax break:

- 1) For the tax break, you are allowed to consider \$3,000 of your expenses for one child or \$6,000 for two or more children. There is a flat limit of \$5,000 for the Section 125 Plan. If you have two children, and \$6,000 of expenses or more, you can elect \$5,000 in the Section 125 Plan, and still claim \$1,000 on your tax return.
- 2) You do not save the Social Security taxes if you take the tax credit.
- 3) The Section 125 Plan does not reduce your savings as your income rises; the tax credit does. You are not penalized for being financially successful.

Who qualifies as a dependent?

- ❖ A child under the age of 13 whom you claim as a dependent on your federal income tax return and who lives with you. If you are divorced, if your child lives with you more days during the year than (s)he lives with the other parent, then (s)he is a qualifying child.
- ❖ A spouse, parent, or other family member who is physically or mentally incapable of caring for himself or herself and is claimed as a dependent on your tax return.

What else do I need to know?

- ❖ Expenses must be incurred during the plan year.
- ❖ Expenses incurred enable you to be gainfully employed. (your spouse must be gainfully employed if you are married)
- ❖ The daycare provider will comply with all applicable state and local laws.
- ❖ The reimbursement may not exceed:
 - The maximum allowed under the plan.
 - \$5,000 if filing a joint tax return or \$2,500 if filing separate returns.
 - Your taxable compensation.
 - If you are married, your spouse's actual or deemed earned income.

How much will I save if I participate in this Plan?

\$100 Bi-Weekly Daycare Expense

Without Flexible Spending

\$700.00 Earnings
 \$105.00 Federal Income Tax
 \$ 53.55 Social Security Tax
 \$100.00 Bi-Weekly Daycare
 \$541.45 Take Home Pay
 \$441.45 Disposable Income

With Flexible Spending

\$700.00 Earnings
 \$ 90.00 Federal Income Tax
 \$ 45.90 Social Security Tax
 \$100.00 Bi-Weekly Daycare
 \$600.00 Taxable Earnings
 \$464.10 Disposable Income

\$22.65 Savings Bi-Weekly
\$588.90 Savings Per Year!

