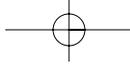
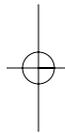
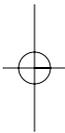
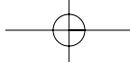


Credit Where Credit is \$ Due

Using Tax Breaks to
Help Pay for Child and
Dependent Care





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2 **7** Eligibility for These Tax Breaks

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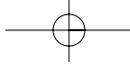


Did you know that you might be eligible for tax breaks to help pay for your child and dependent care expenses and reduce the taxes you pay or increase your tax refund? This booklet is designed to inform you about four of these tax breaks in the federal income tax code: the Dependent Care Tax Credit, the Child Tax Credit, the Earned Income Tax Credit, and the Dependent Care Assistance Program. The information provided here can help you determine if you are eligible to receive the tax assistance these provisions offer for tax year 2001, give you an idea of the amount of tax assistance you can receive and how to claim it, and answer some other questions you may have about these tax breaks. This booklet is not intended to provide legal assistance but to help individuals understand their eligibility for tax breaks.

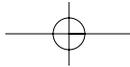
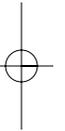
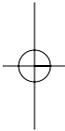
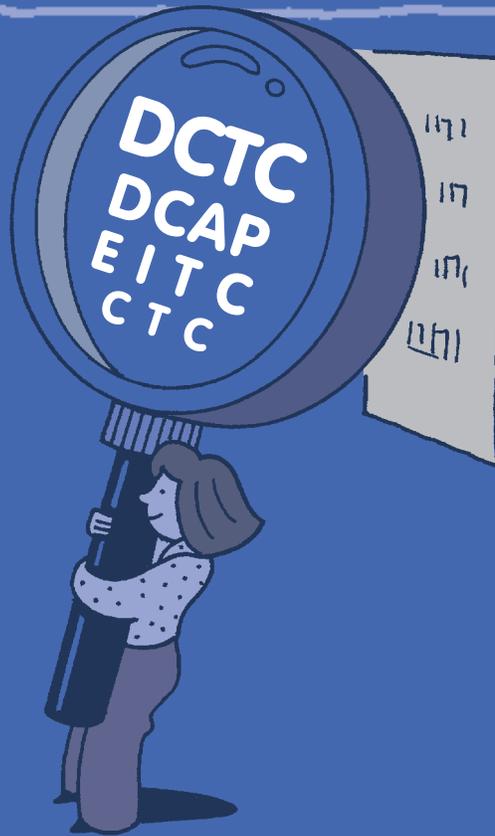
If you are eligible for the Dependent Care Tax Credit, the Child Tax Credit and the Earned Income Tax Credit, you can claim benefits under all three provisions. Under some circumstances you may be able to claim the Dependent Care Tax Credit even if you also receive benefits through a Dependent Care Assistance Program. You can use these tax breaks to reduce the federal income taxes you pay. Even if your income is so low that you don't pay federal income taxes, you may be able to get a tax refund by claiming the refundable Earned Income Tax Credit and/or Child Tax Credit.

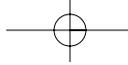
This booklet is organized in four sections:

-  The 2001 Dependent Care Tax Credit, Child Tax Credit, Earned Income Tax Credit, and Dependent Care Assistance Program at a glance;
-  Eligibility for these tax breaks;
-  Help estimating the value of these tax breaks to you; and
-  Information on how to claim these tax breaks, and how to obtain more information about them and similar state tax breaks.



1





Tax Breaks At-A-Glance

3

Dependent Care Tax Credit (DCTC)

The Dependent Care Tax Credit for 2001 can be as much as \$720 if you paid for employment-related care in 2001 for one qualifying child or dependent, and as much as \$1,440 if you paid for employment-related care in 2001 for two or more qualifying children or dependents. In general, the amount of your DCTC depends on:

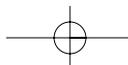
-  your (together with your spouse's, if you are married) adjusted gross income;
-  the number of children or dependents in care;
-  the amount you paid for care; and
-  whether and to what extent you participated in a Dependent Care Assistance Program offered by your employer.

In general, the higher your child and dependent care expenses and the lower your income, the larger your DCTC will be.

Individuals and couples at all income levels are eligible for the DCTC, but if you owe no taxes, you will not benefit from the DCTC. However, even if you owe only a small amount of taxes, claiming the DCTC can increase the amount of any tax refund you may receive.



In general, the higher your child and dependent care expenses and the lower your income, the larger your DCTC will be.



4**Child Tax Credit (CTC)**

The Child Tax Credit for 2001 can be as much as \$600 for each of your qualifying children if you are single and you had 2001 modified adjusted gross income of \$86,000 or less, or if you are married and you (together with your spouse) had 2001 modified adjusted gross income of \$121,000 or less.

If you don't owe federal income taxes or the amount of the CTC for which you are eligible is greater than the amount of federal income taxes you owe, you can receive a refund of some or all of the CTC for which you are eligible if you have at least \$10,000 in earned income for 2001.

Earned Income Tax Credit (EITC)

The Earned Income Tax Credit for 2001 can be as much as:

-  \$2,428 if you have one qualifying child and you (together with your spouse, if you are married) had 2001 earned income and modified adjusted gross income of \$28,281 or less;
-  \$4,008 if you have two or more qualifying children and you (together with your spouse, if you are married) had 2001 earned income and modified adjusted gross income of \$32,121 or less; and
-  \$364 if you have no qualifying children and you (or your spouse, if you are married) were at least age 25 but under age 65 at the end of 2001, and you (and your spouse, if you are married) had 2001 earned income and modified adjusted gross income of \$10,710 or less.

If you have a qualifying child, you can receive a portion of your EITC in advance—that is, in your paycheck each pay period—to help you meet your current expenses.

If you don't owe federal income taxes, or if the amount of the EITC for which you are eligible is greater than the amount of federal income taxes you owe, you can still receive a refund for the difference between the EITC for which you are eligible and the federal income taxes you owe.

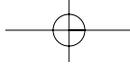
Dependent Care Assistance Program (DCAP)

Employers are permitted to provide eligible employees up to \$5,000 per year in tax-free child and dependent care benefits if the benefits are provided through a Dependent Care Assistance Program. Employees do not have to pay federal income taxes, employers do not have to pay employment taxes, and neither employers nor employees have to pay Social Security and Medicare taxes (also known as "payroll taxes") on benefits offered through a DCAP. In most states, employees do not have to pay state income taxes on these benefits either. In general, the eligibility requirements and the type of care covered under a DCAP are the same as under the DCTC.

Dependent Care Assistance Program benefits may take several forms, including cash reimbursements, vouchers, and the provision of care in an outside child or dependent care facility or in an employer's own child or dependent care facility. These benefits may be fully funded by the employer without requiring any contribution from employees. Most commonly, however, an employer establishes a DCAP as a salary reduction plan, whereby employees are permitted to set aside amounts from their annual salaries to cover their employment-related child and dependent care expenses. A participating employee's pay is reduced by the amount the employee designates (subject to the \$5,000 limitation and sometimes subject to an additional employer limitation), and this amount is returned to the employee in the form of a tax-free reimbursement for child and dependent care expenses. In effect, the assistance received by the employee is the amount of money saved by not paying taxes on the amount by which the employee's pay was reduced. Because most employers provide DCAP benefits funded solely by salary reduction, the illustrations in this booklet focus mostly on DCAP salary-reduction plans.

The size of your CTC or EITC, unlike the DCTC, does not depend upon your incurring any particular expenses but rather depends on your income and the number of children you have.





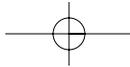
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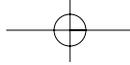
DCTC

EITC

DCAP

CTC





Eligibility for These Tax Breaks

7

This section will help you determine if you can receive these tax breaks by answering some commonly asked questions about eligibility, including questions about the relationship of the tax breaks to each other and to your eligibility for specific government benefit programs.

Who is a qualifying child or dependent for the purpose of claiming the DCTC or receiving DCAP benefits, and a qualifying child for the purpose of claiming the CTC or EITC?

For DCTC/DCAP

A qualifying child is a child under age 13 at the time care was provided who lived with you in 2001 and whom you can claim as a dependent on your 2001 tax return. A qualifying dependent is 1) a disabled individual (including a child older than 13 or a parent) who lived with you in 2001, is physically or mentally incapable of self-care, and whom you claim as a dependent on your 2001 tax return, or 2) a disabled spouse who lived with you in 2001 and is physically or mentally incapable of self-care.

You can claim as a dependent on your 2001 tax return an individual 1) for whom you (and/or your spouse, if you are married) provided more than half of the support for 2001; and 2) who is your (or your spouse's, if you are married) child (grandchild, great-grandchild, etc.), stepchild, sibling, stepsibling, parent (grandparent, great-grandparent, etc.), stepparent, niece, nephew, aunt or uncle, or any individual who lived with you during all of 2001. There are special rules for married, adopted and foster children. Generally, an individual must be a U.S. citizen or resident alien, or a resident of Mexico or Canada, for you to be able to claim that individual as a dependent.



8**For CTC**

A qualifying child is your child (grandchild, great-grandchild, etc.) or stepchild who was under age 17 on December 31, 2001, is a U.S. citizen or resident alien, and is claimed by you as a dependent on your 2001 tax return. There are special rules for married, adopted and foster children.

For EITC

A qualifying child is your child (grandchild, great-grandchild, etc.) or stepchild who lived with you in your main home in the U.S. for more than six months in 2001, and who on December 31, 2001 was under age 19, or under age 24 and a full-time student, or any age and permanently and totally disabled. There are special rules for married, adopted and foster children and for a child who is also the qualifying child of another person.

If I am divorced or separated from my spouse and my ex-spouse claims our child as a dependent, but I have custody of our child or share joint custody with my ex-spouse, can I claim the DCTC or receive DCAP benefits for the care of our child, or claim the CTC or EITC for our child?

For DCTC/DCAP

If you were divorced, legally separated, or lived apart from your spouse during the last six months of 2001, you can claim the DCTC or receive DCAP benefits if you incurred qualifying care expenses for the child and all of the following conditions apply: 1) you had custody of the child for a longer time in 2001 than the other parent; 2) one or both of you provided over half of the child's support in 2001; 3) one or both of you had custody of the child for more than half of 2001; and 4) the other parent claims the child as a dependent because you as the custodial parent signed form 8332 or a similar statement, agreeing not to claim the child as a dependent for 2001.

For CTC/EITC

You must actually claim the child as a dependent in order to claim the CTC for the child, but you do not have to be able to claim the child as a dependent (or actually claim the child as a dependent), in order to claim the EITC for the child.

What is included in income for the purpose of claiming the DCTC, CTC and EITC, or for receiving DCAP benefits?

For DCTC/DCAP

Adjusted gross income is used to determine the amount of your DCTC. Earned income may be used to limit the amount of child and dependent care expenses that you can claim for the DCTC or the benefits you can receive through a DCAP.

For CTC

Modified adjusted gross income is used to determine your eligibility for the CTC. Earned income is used to determine your eligibility for and the amount of your CTC refund.

For EITC

Both earned income and modified adjusted gross income are used to determine your eligibility for and the amount of your EITC.

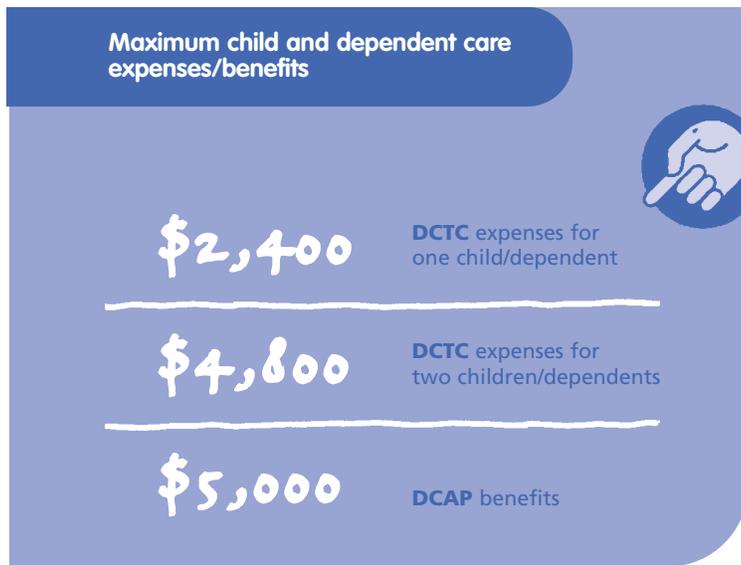
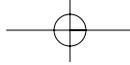
In general, adjusted gross income is gross income, minus certain allowable deductions. It includes wages, salaries and tips and net income from self-employment, as well unemployment compensation, alimony and taxable interest received. It does not include child support payments received or student loan interest and alimony paid. For most people, modified adjusted gross income is the same as adjusted gross income. Earned income is defined differently for the CTC than it is for the DCTC, a DCAP or the EITC. Your tax forms will help you determine what is earned income for each of these tax breaks.

10*What kind of care can I use to claim the DCTC or to receive benefits through a DCAP?*

All types of child or dependent care—including in a center, a church, or a family or adult day care home, or by a neighbor or relative (except care provided by your spouse or dependent, or your child who was under the age of 19 on December 31, 2001)—qualify as long as you paid for the care and the care was necessary for you to work or look for work in paid employment. If you are married, both you and your spouse must have needed the care to work or look for work, or one spouse must have been a full-time student or incapable of self-care. The care does not include schooling for a child in the first grade or above, or overnight camp. However, it does include after-school programs and day camp during school vacations. In addition, if the care was provided in a place that provides care for more than six persons, the provider must meet all applicable state and local regulations. In the case of a dependent, the care must be for an individual who regularly spends at least eight hours a day in the home of the person claiming the DCTC or benefiting from a DCAP, so care in a residential care facility (such as a nursing home) for spouses or other individuals who are incapable of self-care, is not eligible.

Most types of child or dependent care qualify as long as you paid for the care and the care was necessary for you to work or look for work in paid employment.

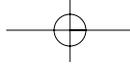




Are there limits on the child and dependent care expenses that I can claim for the DCTC or the benefits that I can receive through a DCAP?

You (and your spouse, if you are married) may not claim more than \$2,400 in care expenses for one child or dependent or \$4,800 in care expenses for two or more children or dependents for the DCTC, or receive more than \$5,000 in benefits through a DCAP for 2001. (Your DCAP benefits are also subject to limitations that may be imposed by your employer, including limitations necessary to comply with the requirement that a DCAP not discriminate in favor of highly compensated employees.) In the case of both the DCTC and a DCAP, the care expenses you claim must be less than your 2001 earned income. If you are married, the expenses you claim must be less than your 2001 earned income or your spouse's 2001 earned income, whichever is smaller. There are special rules for calculating the earned income of a spouse who was a full-time student or incapable of self-care.





May I claim the DCTC if I receive benefits under a DCAP?

Sometimes. If you participate in a DCAP, the amount of money you receive through the DCAP must be subtracted from the child and dependent care expenses you can use to calculate the DCTC. For example, if your employer provides you with \$1,500 through a DCAP (through salary reduction or otherwise) for 2001 child care expenses, and you incur \$2,000 in child care expenses in 2001, you could only claim the DCTC for \$500 of your 2001 child care expenses. Similarly, because only the first \$2,400 of care expenses for one child or dependent and the first \$4,800 of care expenses for two or more children or dependents can serve as the basis for claiming the DCTC in 2001, if you receive more than \$2,400 in 2001 DCAP benefits for one child or dependent or more than \$4,800 in 2001 DCAP benefits for two or more children or dependents, you cannot claim the DCTC for 2001. Finally, if all of your 2001 child and dependent care expenses are covered by benefits received through a DCAP in 2001, you cannot claim the DCTC for 2001. Especially if an employer offers DCAP benefits only as a salary reduction, and depending on the amount of care expenses incurred, it can be more advantageous for lower- and middle-income families to claim the DCTC than to participate in a DCAP, and it can be more advantageous for higher-income families to participate in a DCAP than to claim the DCTC.

Sometimes you can both participate in a DCAP and receive the DCTC.

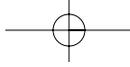


What happens if I spend less on child and dependent care than the amount of my salary reduction for child and dependent care expenses under a DCAP?

In general, if you do not use the full amount that you designated for salary reduction at the beginning of the plan year for child or dependent care expenses over the course of the year, you will lose the right to receive the “leftover” money. This is sometimes referred to as the “use it or lose it” rule and means that it is important to be careful when designating the amount of salary reduction that you want.

Will my CTC or EITC refund affect my eligibility to receive government benefits?

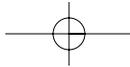
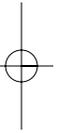
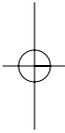
Usually, no. The amount of your CTC and EITC refunds will not be used to determine if you are eligible for Medicaid, Supplemental Security Income (SSI), Food Stamps or low-income housing, nor will they be used to determine how much you can receive from those programs. Your CTC refund also will not be used to determine if you are eligible for, or how much you will receive in, Temporary Assistance for Needy Families (TANF) benefits. Each state is permitted to develop its own rules on whether the EITC refund will be used to determine eligibility for and the amount of TANF benefits, so be sure to check with your state TANF agency for the EITC rules in your state.

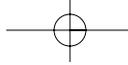


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EITC
DCAP
CTC
DCTC





Determining the Value of the Tax Breaks

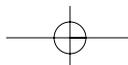
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This section shows you how to estimate how much you can get from the four tax breaks and estimates the benefits for two sample families as illustrations. These are only approximations; the actual amounts you can receive will depend on your individual circumstances.

How much can I get through the DCTC and/or a DCAP?

The amount you can get through the DCTC depends on your income, the number of children or dependents in care, and the amount you paid for care. It also depends on whether and to what extent you participated in a DCAP.

The DCTC is calculated as a percentage of qualifying child and dependent care expenses. Qualifying expenses for 2001 may not exceed \$2,400 for one child or dependent and \$4,800 for two or more children or dependents. Individuals and couples with 2001 adjusted gross incomes of less than \$10,000 receive a credit equal to 30 percent of eligible expenses, for a maximum of \$1,440. The rate decreases as adjusted gross income increases above \$10,000 until it reaches 20 percent for individuals and couples with adjusted gross incomes above \$28,000.



The following tables give you a general idea of how much the DCTC is worth to you by showing the amount of the DCTC available for individuals and couples at different income levels with varying child or dependent care expenses. To determine the amount of the DCTC you can expect to receive, first choose the table that applies to your situation: Table 1 if you have one child or dependent, Table 2 if you have two or more children or dependents. Look down the first column to find the dollar range in which your 2001 adjusted gross income falls. Then read across that row to the column that most closely matches the amount you spent on child or dependent care during 2001 to find the DCTC you can expect to receive.

TABLE 1

Sample Child and Dependent Care Tax Credit Amounts for an Individual/Couple with One Child or Dependent, Tax Year 2001

Adjusted Gross Income	Care Expenses for One Child or Dependent			
	\$1,000	\$1,500	\$2,000	\$2,400+
\$0-10,000	\$300	\$450	\$600	\$720
\$10,001-12,000	\$290	\$435	\$580	\$696
\$12,001-14,000	\$280	\$420	\$560	\$672
\$14,001-16,000	\$270	\$405	\$540	\$648
\$16,001-18,000	\$260	\$390	\$520	\$624
\$18,001-20,000	\$250	\$375	\$500	\$600
\$20,001-22,000	\$240	\$360	\$480	\$576
\$22,001-24,000	\$230	\$345	\$460	\$552
\$24,001-26,000	\$220	\$330	\$440	\$528
\$26,001-28,000	\$210	\$315	\$420	\$504
\$28,001+	\$200	\$300	\$400	\$480

TABLE 2

Sample Child and Dependent Care Tax Credit Amounts for an Individual/Couple with Two or More Children or Dependents, Tax Year 2001

Adjusted Gross Income	Care Expenses for Two Children or Dependents				
	\$1,000	\$2,000	\$3,000	\$4,000	\$4,800+
\$0-10,000	\$300	\$600	\$900	\$1,200	\$1,440
\$10,001-12,000	\$290	\$580	\$870	\$1,160	\$1,392
\$12,001-14,000	\$280	\$560	\$840	\$1,120	\$1,344
\$14,001-16,000	\$270	\$540	\$810	\$1,080	\$1,296
\$16,001-18,000	\$260	\$520	\$780	\$1,040	\$1,248
\$18,001-20,000	\$250	\$500	\$750	\$1,000	\$1,200
\$20,001-22,000	\$240	\$480	\$720	\$960	\$1,152
\$22,001-24,000	\$230	\$460	\$690	\$920	\$1,104
\$24,001-26,000	\$220	\$440	\$660	\$880	\$1,056
\$26,001-28,000	\$210	\$420	\$630	\$840	\$1,008
\$28,001+	\$200	\$400	\$600	\$800	\$960

You may find that the exact amount you spent on child or dependent care is not listed. If this is the case, the table will provide you with the dollar range in which your DCTC will fall. Find your 2001 adjusted gross income level in the first column of the table and read across to the columns just below and just above the amount you spent. Your DCTC will fall between the two amounts listed. If, for example, your 2001 adjusted gross income was \$40,000, your child care expenses were \$2,200 in 2001 and you have one child, your 2001 DCTC would be between \$400 and \$480.

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If your employer offers a DCAP and you participated in that program in 2001, the amount you can get from the DCTC will be less than the amount shown on these tables since you must subtract any DCAP benefits you received from the expenses you can use to calculate the DCTC. For example, if you received \$2,200 in DCAP benefits from your employer and had \$2,200 in child care expenses in 2001, you cannot claim the DCTC.

The amount of tax savings you can receive by participating in a DCAP depends on the amount of DCAP benefits you receive from your employer (whether through salary reduction or otherwise), since you do not pay taxes on these benefits. To determine the amount of your tax savings, you must first determine your marginal income and payroll tax rates. Your marginal tax rates are the tax rates you pay on your last dollar of income.

Tables 3 and 4 give you a general idea of the federal marginal income and payroll tax rates for 2001. To estimate your federal marginal income tax rate, read down the first two columns of Table 3 and find the dollar range in which your 2001 adjusted gross income falls. Then read across that row to find your 2001 marginal income tax rate. To estimate your federal marginal payroll tax rate, read down the first two columns of Table 4 and find the dollar range in which your 2001 earnings fall. Then read across that row to find your 2001 marginal payroll tax rate. For example, if you earned \$40,000 in 2001, your federal marginal income tax rate would be 15 percent and your federal marginal payroll tax rate would be 7.65 percent.



The amount of tax savings you can receive by participating in a DCAP depends on the amount of DCAP benefits you receive from your employer (whether through salary reduction or otherwise), since you do not pay taxes on these benefits.

TABLE 3

Approximate Federal Marginal Income Tax Rates for 2001 for Families with One or Two Children

If your AGI is greater than...	But less than...	Your marginal income tax rate is...
0	\$25,000	10%
\$25,000	\$60,000	15%
\$60,000	\$120,000	27.5%
\$120,000	\$180,000	30.5%
\$180,000	\$320,000	35.5%
\$320,000		39.1%

This table assumes that tax filers claim the standard deduction and the personal exemption and that tax filers have one or two children. If you itemize your deductions, have income too high to benefit from the personal exemption, or have more than two children, this table will not accurately reflect your marginal tax rate.

TABLE 4

Federal Marginal Payroll Tax Rates for 2001

If your earnings are greater than...	But less than...	Your marginal payroll tax rate is...
0	\$80,400	7.65%
\$80,400		1.45%

The payroll tax assessed on workers is 7.65% of earnings below \$80,400 and 1.45% of earnings above \$80,400.

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You may also receive some state tax savings from participating in a DCAP; the amount you save will depend on your state marginal tax rate.

You can estimate your federal tax savings from participating in a DCAP by multiplying the amount of DCAP benefits you receive from your employer by your marginal tax rates. For example, if you have a marginal income tax rate of 15 percent, a marginal payroll tax rate of 7.65 percent, and \$5,000 in DCAP benefits, you would receive \$750 ($\$5,000 \times 0.15$) in federal income tax savings and \$383 ($\$5,000 \times 0.0765$) in federal payroll tax savings. Adding these figures together gives you a rough estimate of your federal tax savings—\$1,133—from participating in a DCAP.

The value to you of participating in your employer's DCAP will be greater than these tax savings if you receive DCAP benefits over and above your full salary (that is, if your employer provides you with DCAP benefits that are not funded by salary reduction). In that instance, you would add the amount of these benefits to your tax savings to determine the full value of participating in the DCAP.

If you have no tax liability you will not be able to benefit from the DCTC, and if your tax liability is low, you may not be able to benefit from the full amount of the DCTC for which you are otherwise eligible. This is because the DCTC, unlike the CTC and the EITC, is not refundable. Similarly, you will receive no tax savings from participating in a DCAP if you have no tax liability, and if your tax liability is low, you may not be able to benefit fully from the tax savings otherwise available through a DCAP. (You will still benefit from participating, however, if your employer offers you a DCAP that is not a salary reduction plan, since in that instance your employer will be providing you with child and dependent care benefits in addition to your salary.) In general, a single parent with one child and adjusted gross income less than \$12,450 and a married couple with two children and adjusted gross income less than \$19,200 owe no federal income taxes. Because it is difficult to predict your tax liability at the time that you have to decide whether to participate in a DCAP, you should calculate your potential savings from participating in a DCAP as if you had tax liability, comparing that to your potential tax savings from claiming the DCTC, to decide which is more beneficial to you.

Finally, it is important to remember that when you set aside part of your salary in a DCAP, you reduce the amount of earnings credited to you for the purpose of determining the amount of your Social Security benefits. Although this could have some effect on the Social Security benefits you receive in the future, for most individuals the effect is very modest.

The following examples illustrate how two sample families can use these tables to determine their tax savings from claiming the DCTC and participating in a DCAP.

Sample Family Profiles

Natalie is a single mother who files her tax return as a head of household. She has one child under age 13, works part-time, earned \$20,000, and spent \$1,500 on work-related child care expenses during 2001. Natalie's employer offers a DCAP salary-reduction plan but Natalie does not participate in the plan.

Lesley and Harold are married and file a joint tax return. They have two children under age 13, both work full-time, earned \$70,000, and spent \$5,000 on child care expenses during 2001. Lesley's employer offers a DCAP salary-reduction plan. She set aside \$5,000 of her salary in 2001 to pay for child care expenses.

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Example

DCTC vs. DCAP

DCTC		\$375
<hr/>		
DCAP benefit		\$1,500
federal marginal income tax rate	X	.10
	=	\$150
DCAP benefit		\$1,500
federal marginal payroll tax rate	X	.0765
	=	\$115
\$150 + \$115	=	\$265

Natalie receives more from the DCTC



Natalie and the DCTC/DCAP

Table 1 shows that at Natalie’s income level and \$1,500 in child care expenses, she can expect \$375 from the DCTC. Because Natalie did not participate in her employer’s DCAP, she does not have any DCAP benefits to subtract from the child care expenses she can use to claim the DCTC. Her DCTC of \$375 will therefore lower her federal income taxes by that amount.

If Natalie had participated in her employer’s DCAP and received \$1,500 in benefits for child care expenses through that plan for 2001, the value to her of participating in the DCAP would be the amount of the 2001 federal income taxes and federal payroll taxes she would have paid on \$1,500 if she had received that amount as salary. Table 3 shows that at her income level the federal marginal income tax rate is 10 percent. Multiplying her \$1,500 in DCAP benefits by this tax rate yields a federal income tax savings of \$150 (\$1,500 x 0.10). Table 4 shows that at her income level the federal marginal payroll tax rate is 7.65 percent. Multiplying her \$1,500 in DCAP benefits by this tax rate yields a federal marginal payroll tax savings of \$115 (\$1,500 x 0.0765). Her total federal tax savings would be \$265 (\$150 in federal income taxes and \$115 in federal payroll taxes). Because this amount (at least before any state tax savings are taken into account) is less than the amount Natalie would receive through the DCTC for 2001 (\$375), it is more beneficial for her to claim the DCTC than to participate in her employer’s DCAP. This example shows why it is important to estimate whether you would do better by participating in a DCAP or by claiming the DCTC before you sign up to participate in a DCAP.

Lesley and Harold and the DCTC/DCAP

Lesley set aside \$5,000 of her salary in her employer's DCAP and received that amount in benefits to pay for child care expenses in 2001. Because this amount is more than the maximum expenses Lesley and Harold can use to claim the DCTC for 2001 (\$4,800), they cannot claim the DCTC.

The value of Lesley and Harold's 2001 DCAP benefits is the amount they save by not paying 2001 taxes on the \$5,000. Table 3 shows that at their income level the federal marginal income tax rate is 27.5 percent. Multiplying their \$5,000 in DCAP benefits by this tax rate yields a federal income tax savings of \$1,375 ($\$5,000 \times 0.275$). Table 4 shows that at their income level the marginal federal payroll tax rate is 7.65 percent. Multiplying their \$5,000 in DCAP benefits by this tax rate yields a federal payroll tax savings of \$383 ($\$5,000 \times 0.0765$). Leslie and Harold's total federal tax savings would be \$1,758 (\$1,375 in federal income taxes and \$383 in federal payroll taxes) from participating in the DCAP salary reduction plan offered by Lesley's employer.

If Lesley and Harold had chosen not to participate in the DCAP, they could instead claim the DCTC for 2001. They would receive a 2001 tax benefit of \$960 through the DCTC. Lesley and Harold receive more through the DCAP (even before any state tax savings are taken into account) than they would receive if they claimed the DCTC instead.

While neither of the families in these examples both claimed the DCTC and participated in a DCAP, a family could qualify for and benefit from both. For example, if Lesley and Harold had set aside only \$3,000 in a DCAP to pay for their \$5,000 in 2001 child care expenses, they would also be able to claim the DCTC for 2001 since the amount of 2001 DCAP benefits they received would not exceed the maximum amount of expenses they could claim for the DCTC (\$4,800). After subtracting the \$3,000 from the \$4,800 expense limit, they would have \$1,800 in child care expenses to use when claiming the DCTC. They would receive \$400 in 2001 tax savings from the DCTC and their 2001 tax savings from setting aside the \$3,000 in a DCAP would be \$1,055 (\$825 in federal income tax savings and \$230 in federal payroll tax savings). Their total federal tax savings would be \$1,455.

Example

DCTC vs. DCAP

DCTC	\$960
DCAP benefit	\$5,000
federal marginal income tax rate	X .275
= \$1,375	
DCAP benefit	\$1,500
federal marginal payroll tax rate	X .0765
= \$383	
\$1,375 + \$383 = \$1,758	

Leslie and Harold receive more from a DCAP

How much can I get through the CTC?

The amount you can get through the CTC depends on the number of children in your family and your income.

The CTC can be as much as \$600 per child for single individuals with 2001 modified adjusted gross income below \$75,000 and married couples with 2001 modified adjusted gross income below \$110,000. The CTC gradually decreases for individuals and couples with modified adjusted gross income above these amounts, until it reaches zero for single individuals with modified adjusted gross income above \$86,000 and married couples with modified adjusted gross income above \$121,000.

To determine how much you can receive from the CTC for 2001, multiply \$600 by the number of children you have. You will receive less than this amount if you have 2001 modified adjusted gross income above \$75,000 if you are single or \$110,000 if you are married.

Even if you pay little or no federal income taxes, you can receive all or part of the CTC as a refund, if you have sufficient earned income. Determining what this refund may be is fairly complicated to do on your own, but your tax forms walk you through the calculation. In brief, if all or some portion of the CTC is unused because the amount of your CTC exceeds the amount of taxes you owe, a further calculation is necessary to determine if you can receive all or part of the CTC as a refund. The refund you can receive for 2001 is equal to either 1) the unused portion of your CTC or 2) 10% of your (and, your spouse's, if you are married) 2001 earned income over \$10,000, whichever is less. Special rules apply for determining the CTC refund for families with three or more children.



The CTC can be as much as \$600 per child for single individuals with 2001 modified adjusted gross income below \$86,000 and married couples with 2001 modified adjusted gross income below \$121,000.

Natalie and the CTC

Natalie, who has one child and modified adjusted gross income and earned income of \$20,000, would receive a CTC of \$600 for 2001. However, her income is so low that after claiming the DCTC she only owes \$380 in taxes. Subtracting \$380 from \$600 leaves her with an unused CTC of \$220. Her 2001 earned income of \$20,000 is above the \$10,000 threshold for claiming a CTC refund, so she is entitled to a refund, calculated as described above. Ten percent of her earned income above \$10,000 ($\$10,000 \times 0.10$) is \$1,000. Since this amount is more than her unused CTC of \$220, she would receive a CTC refund of \$220.

Lesley and Harold and the CTC

Lesley and Harold, who have two children and modified adjusted gross and earned income of \$70,000, would receive a CTC of \$1,200 ($\600×2) for 2001.

The CTC and EITC are available whether or not you have incurred any particular expenses, and can be received as a refund if you have little or no tax liability.



How much can I get through the EITC?

The amount you can get through the EITC depends on your income and the number of children in your family.

You can use Table 5 on page 26 to get an idea of how much you can receive from the EITC for 2001. Read down the first column until you find the dollar amount closest to your income level. Then read across that row to the column that applies to the number of children in your family to find the approximate amount you can expect to receive from the EITC. If your income level falls between two of the dollar amounts listed you can see the dollar range in which your EITC benefits will fall by reading across the rows for the income levels just above and just below your own. If, for example, you have one qualifying child and your 2001 earned income totaled \$19,000, your EITC would be between \$1,324 and \$1,643.

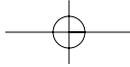


TABLE 5

Earned Income Tax Credit Amounts, Tax Year 2001

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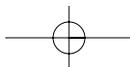
Earned Income / Modified AGI	One qualifying child	Two or more qualifying children	No qualifying children	Earned Income / Modified AGI	One qualifying child	Two or more qualifying children	No qualifying children
\$0	\$0	\$0	\$0	\$18,000	\$1,643	\$2,974	\$0
\$2,000	\$680	\$800	\$153	\$20,000	\$1,324	\$2,553	\$0
\$4,000	\$1,360	\$1,600	\$306	\$22,000	\$1,004	\$2,132	\$0
\$6,000	\$2,040	\$2,400	\$360	\$24,000	\$685	\$1,710	\$0
\$8,000	\$2,428	\$3,200	\$207	\$26,000	\$365	\$1,289	\$0
\$10,000	\$2,428	\$4,000	\$54	\$28,000	\$45	\$868	\$0
\$12,000	\$2,428	\$4,008	\$0	\$30,000	\$0	\$447	\$0
\$14,000	\$2,283	\$3,816	\$0	\$32,000	\$0	\$26	\$0
\$16,000	\$1,963	\$3,395	\$0	\$34,000+	\$0	\$0	\$0

Natalie and the EITC

Natalie can expect to receive \$1,324 from the EITC for 2001. Reading across the row for \$20,000 in income, a family with one child would receive \$1,324.

Lesley and Harold and the EITC

Lesley and Harold are not eligible for the EITC because their 2001 earned income is too high. Reading across the row for \$34,000+ in income, a family with two children would receive \$0.



What is the combined value of these tax benefits?

You can claim the DCTC, CTC and EITC if you meet the eligibility requirements for each provision. As noted above, if you participate in a DCAP, your DCTC will be affected. If you receive less in DCAP benefits from your employer than you paid in child or dependent care expenses and your DCAP benefits are less than your maximum DCTC expense limit, then you can both claim the DCTC and participate in a DCAP. The expenses you can claim for the DCTC, however, will be reduced by the amount of the DCAP benefits you receive.

Natalie can receive \$2,299 in 2001 federal tax savings by claiming the DCTC, the CTC and the EITC.

Natalie will use her entire DCTC and \$380 of her CTC to wipe out her tax liability. She will receive \$220 from the CTC and \$1,324 from the EITC as a refund, for a total refund of \$1,544.

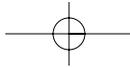
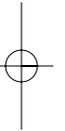
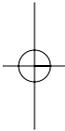
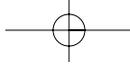
Example	
Natalie's Tax Savings	
DCTC	\$375
CTC	+ \$600
EITC	+ \$1,324
<hr/>	
Total federal tax savings	= \$2,299

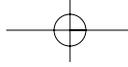


Example	
Leslie and Harold's Tax Savings	
DCTC	\$0
DCAP	+ \$1,758
CTC	+ \$1,200
EITC	+ \$0
<hr/>	
Total federal tax savings	= \$2,958



Lesley and Harold, who are not eligible for the EITC, can receive \$2,958 in 2001 federal tax savings by participating in a DCAP and claiming the CTC.





How to Claim the Tax Breaks and Get More Information About Them and Similar State Tax Breaks

What do I need to do to claim the DCTC or to receive benefits through a DCAP?

To claim the DCTC, you must file a tax return. You must file either tax form 1040 or 1040A (not 1040EZ) and a separate form or schedule with your tax return. With tax form 1040, file form 2441. With tax form 1040A, file Schedule 2. Note that these forms refer to the DCTC as the “Credit for Child and Dependent Care Expenses.”

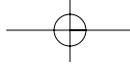
To benefit from a DCAP, your employer must offer a DCAP and you must participate in it. You must also report the amount of your DCAP benefits on your tax return. You must file either tax form 1040 or 1040A (not 1040EZ) and form 2441 (with form 1040) or Schedule 2 (with form 1040A). The amount of any DCAP benefits you received during 2001 should be provided by your employer in Box 10 of your W-2 form.

To claim the DCTC or benefit from a DCAP, you must provide a Social Security number for any qualifying child or dependent. To get a Social Security number, contact your local Social Security Administration office or call the Social Security Administration's toll-free number, 1-800-772-1213. If you were married at the end of 2001, you generally must file a joint return, although special rules apply if you lived apart from your spouse.

To claim the DCTC or benefit from a DCAP, you must also have basic information about your provider, including the provider's name, address, and, if the provider is not a tax-exempt organization, an identification number (the provider's Social Security number or employer identification number). If you have tried to get your provider's identification number but have not been successful, you can explain on your return that you asked for the information but the provider did not comply with your request.

What do I need to do to claim the CTC?

Even if you don't owe any federal income taxes, you must file a tax return to claim the CTC. You must file either tax form 1040 or 1040A (not 1040EZ). You must provide a Social Security number for any qualifying child. If your adjusted gross income is above \$75,000 (if you are single) or above \$110,000 (together with your spouse's adjusted gross income, if you are married), you must also file form 972. To claim the refundable component of the CTC, you must also file form 8812.



What do I need to do to claim the EITC?

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Even if you don't owe any federal income taxes, you must file a tax return to claim the EITC. If you have a qualifying child, you must file either tax form 1040 or 1040A (not 1040EZ) and a separate form, Schedule EIC. If you have no qualifying children, you may file either form 1040, 1040A or 1040EZ. If you were married at the end of 2001, you must file a joint return. You must provide a Social Security number for any qualifying child. If you can provide the basic information to show your eligibility, the IRS will calculate your EITC for you.

To receive a portion of your EITC in advance—that is, in your pay-check each pay period—complete tax form W-5 and give it to your employer. You can give form W-5 to your employer at any time during the year, but you should do so as early in the year as possible to begin receiving advance EITC benefits promptly. If you receive advance EITC benefits, you must file a tax return at the end of the year, in order to receive the rest of your EITC benefits. Remember that you must have a qualifying child to receive advance EITC benefits. Remember also, if you elect to receive advance EITC benefits, the amount of any tax refund you could be eligible for at the end of the year will be lower than if you had waited to take all of the EITC when you file your return.

How can I get more information about these tax breaks and similar state tax breaks ?

For more information on the federal tax breaks, you can call the Internal Revenue Service at 1-800-TAX-1040 toll free or contact your local IRS Regional Manager for a current list of Volunteer Income Tax Assistance (VITA) clinics where you can get free help in filing your tax return. You can also visit the IRS website, which provides tax forms, instructions, and other publications to assist you in filing your return, www.irs.gov.

To determine if your state offers similar credits, check with your state department of revenue or the instructions for your state income tax return, or visit www.taxadmin.org/fta/link/link.html, which provides links to state departments of revenue and tax forms for all the states. The National Women's Law Center's publication, *Making Care Less Taxing*, provides information on state child and dependent care credits and deductions, available at www.nwlc.org/mclt; the Center on Budget and Policy Priorities' paper, *A Hand Up*, provides information on state earned income tax credits, available at www.cbpp.org/10-18-01sfp.htm.

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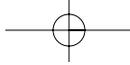


TABLE 2

Sample Child and Dependent Care Tax Credit Amounts for an Individual/Couple with Two or More Children or Dependents, Tax Year 2001

Adjusted Gross Income	Care Expenses for Two Children or Dependents				
	\$1,000	\$2,000	\$3,000	\$4,000	\$4,800+
\$0-10,000	\$300	\$600	\$900	\$1,200	\$1,440
\$10,001-12,000	\$290	\$580	\$870	\$1,160	\$1,392
\$12,001-14,000	\$280	\$560	\$840	\$1,120	\$1,344
\$14,001-16,000	\$270	\$540	\$810	\$1,080	\$1,296
\$16,001-18,000	\$260	\$520	\$780	\$1,040	\$1,248
\$18,001-20,000	\$250	\$500	\$750	\$1,000	\$1,200
\$20,001-22,000	\$240	\$480	\$720	\$960	\$1,152
\$22,001-24,000	\$230	\$460	\$690	\$920	\$1,104
\$24,001-26,000	\$220	\$440	\$660	\$880	\$1,056
\$26,001-28,000	\$210	\$420	\$630	\$840	\$1,008
\$28,001+	\$200	\$400	\$600	\$800	\$960

