

TAX & BUDGET

Improving the Child and Dependent Care Tax Credit Would Help Working Families and Promote Tax Fairness for Women

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For over 60 years, Congress has recognized that the child care expenses parents incur in order to earn income should be acknowledged in the tax code.¹ The Obama Administration and several Members of Congress have proposed strengthening the Child and Dependent Care Tax Credit (CDCTC) to reflect the needs of the increased number of mothers of young children in the labor force and the rising costs of child care.

Child care is a major expense for working families.

- The average fee for full-time child care ranges from over \$3,700 to over \$17,000 per year, depending on location, the type of care, and age of child.
- For example, the average fee for full-time center care for an infant ranges from \$4,800 per year in Mississippi and over \$17,000 per year in Massachusetts.²

Child care consumes a larger share of the budgets of lower-income families.

Families who pay for child care for children under 5 spend, on average:

- 36 percent of their incomes if they are below the federal poverty level;
- 20 percent, if they are between 100 to 200 percent of the poverty level; and
- 8 percent, if they are at or above 200 percent of the poverty level.³

The high cost of child care can discourage women's full participation in the labor force.

Child care expenses can represent a particular barrier to women's participation in the paid labor force, because they consume a substantially larger share of the income of employed mothers than they do of family income overall. The cost of child care relative to the income of working mothers in families who pay for child care for children under five is, on average:

- 43 percent, for mothers with incomes below the poverty level;
- 33 percent, for mothers with incomes between 100 and 200 percent of the poverty level; and
- 21 percent, for mothers with incomes at or above 200 percent of the poverty level.⁴

The current CDCTC provides limited benefits to low-income families because it is not refundable.

In 2014, the CDCTC provided \$3.6 billion in child care assistance to 6.4 million families.⁵ However, even

though on paper the lowest-income families are eligible for the largest credit, they receive only a small share of the tax benefits,⁶ because the credit can only be used to offset federal income tax liability.

The CDCTC allows parents to claim a percentage of their work-related child and dependent care expenses toward the credit: up to \$3,000 for one child or dependent, and up to \$6,000 for two or more children or dependents. The percentage of eligible expenses that a family may claim declines with income. Families with an Adjusted Gross Income (AGI) of \$15,000 or less are eligible for a credit equal to 35 percent of eligible expenses. The rate decreases as AGI increases above \$15,000 until it reaches 20 percent for families with AGIs above \$43,000.

Thus, in theory, families with AGI of \$15,000 or less are eligible for a maximum credit of \$2,100—while families with incomes above \$43,000 are eligible for a maximum credit of \$1,200. However, because the CDCTC is not refundable, many low-income families get little or no benefit from the credit. For example, assuming these families claim the standard deduction and appropriate personal exemptions in 2015:

- A single mother with two children, an AGI of \$20,000, and child care expenses of \$6,000 is theoretically entitled to a CDCTC of \$1,920. However, her federal income tax liability, before credits, is zero, so she is not eligible for any benefit.
- A married couple with two children, an AGI of \$30,000, and child care expenses of \$6,000 is theoretically entitled to a CDCTC of \$1,620. But they would receive only \$140 because their federal income tax liability is \$140.

The current CDCTC loses value over time because its parameters are not indexed for inflation.

- The child care expense limits, currently \$3,000 for one child or dependent and \$6,000 for two or more children or dependents, are not indexed for inflation. They were last increased in 2001 and do not reflect the current costs of child care.⁷

- The sliding scale, last increased in 2001, starts reducing the credit at an AGI of \$15,001 and phases down to its minimum level at \$43,001. It also is not indexed for inflation. As a result, the credit starts shrinking when family income is well below the federal poverty guidelines for a family of three in 2015,⁸ and provides a diminished tax benefit to moderate-income families who may not be eligible for any other type of child care assistance.⁹

The federal CDCTC should be improved to help the families who need it most.

There are several ways to improve the CDCTC to help families who struggle to pay for the child care they need to earn a living:

- **Make the CDCTC refundable.** This crucial reform would allow many low-income working families to claim the credit for the first time and would increase the value of the credit for many moderate-income families.
- **Increase the percentage of expenses that low- and moderate-income families may claim.** Increasing the percentage of expenses that the lowest-income families can claim and raising the income level at which the phase-down begins would increase tax assistance to families who most need help paying for child care.
- **Increase the child care expense limits.** An adjustment would reflect the rise in the cost of child care and help families at all income levels whose expenses exceed the current limits.
- **Index the expense limits and income levels on the sliding scale for inflation.** This would prevent the value of the credit from eroding over time.

Improving the CDCTC would significantly promote tax equity for women.

Women continue to bear the bulk of responsibility for care of children and adult dependents. Tax provisions that help pay for child and dependent care relieve women of some of the burden of unpaid caregiving and lessen barriers to women's participation in the workforce, helping them support themselves and their families.

- 1 In 1954, the tax code provided a deduction for certain work-related child care expenses; the deduction was converted to a credit in 1976 and increased in 1981 and 2001.
- 2 See Child Care Aware of America, Parents and the High Cost of Child Care: 2015 Report (citing the average cost of child care for infants in child care centers in 2014 as ranging between \$4,800 and \$17,000; the average cost of child care for four-year-olds in child care centers in 2014 as ranging between \$4,000 and \$12,700; the average cost of child care for infants in family day care homes as ranging between \$4,000 and \$10,700; and the average cost of child care for four-year-olds in family day care homes as ranging between \$3,700 and about \$10,000), available at <http://usa.childcareaware.org/wp-content/uploads/2015/12/Parents-and-the-High-Cost-of-Child-Care-2015-FINAL.pdf> [hereinafter High Cost of Child Care: 2015]
- 3 U.S. Census Bureau, Who's Minding the Kids? Child Care Arrangements: Spring 2011 (Apr. 2013), Detailed Tables, Table 6, available at <http://www.census.gov/hhes/childcare/data/sipp/2011/tables.html>.
- 4 *Id.*
- 5 Internal Revenue Service, Statistics of Income, Table 1, Individual Income Tax Returns, Tax Year 2014 Preliminary Data: Selected Income and Tax Items by Size of Adjusted Gross Income, available at <https://www.irs.gov/uac/SOI-Tax-Stats-Individual-Income-Tax>Returns#prelim> (last visited Feb 2, 2016).
- 6 Families with incomes below \$30,000 received about 8 percent of the CDCTC tax benefits. See U.S. Department of Treasury, Office of Tax Analysis, Child Care Tax Benefits in 2016, Table 3: Families Benefiting and Amount of Benefit from the Child and Dependent Care Tax Credit: Tax Year 2016, available at <http://www.treasury.gov/resource-center/tax-policy/Documents/OTAR-Child-Care-Tax-Benefits-in-2016.pdf>.
- 7 High Cost of Care: 2015, *supra*, note 2.
- 8 Federal Register, Annual Update of the HHS Federal Poverty Guidelines (Jan. 22 2015) (listing poverty threshold for family of three as \$20,090 and for family of four as \$24,250), available at <https://www.federalregister.gov/articles/2015/01/22/2015-0111201/annual-update-of-the-hhs-poverty-guidelines>.
- 9 See NWLC, Building Blocks: State Child Care Assistance Policies 2015 at 8, available at http://nwlc.org/wp-content/uploads/2015/11/CC_RP_Building_Blocks_Assistance_Policies_2015.pdf (finding that, in 17 states, a family of three earning above \$30,135 a year would be ineligible for child care assistance).