

Frequently Asked Questions

Q. Why might I be taxed?

A. Title 26, United States Code, section 61 and title 26, Code of Federal Regulations, section 1.61-1, Internal Revenue Code (IRC), provide that child care subsidies are generally treated as cash income. This cash income is generally calculated by adding the value of the subsidy to the taxable income of civilian employees who benefit from the subsidies.

Q. What are the next steps?

A. The installation-based child development program director is required to provide each civilian sponsor the cash value of the child care space utilized by a child regardless of age. The cash value of the child care spaces is also provided to the Internal Revenue Service (IRS). The value of the space is determined using a formula that accounts for appropriated fund support and the number of child care spaces available within the child development system of care. The cash value of the subsidy for tax purposes is unique and may vary slightly each year.

Q. What information will I be required to furnish?

A. You will be required to furnish your Social Security number and the names of your dependent children who receive child care through a DoD child care program. This information will be provided to a Third Party Administrator (TPA) who will maintain program information relevant to child care subsidies. The TPA will forward appropriate information to the Defense Finance and Accounting Service (DFAS) who in turn will report child care subsidies on your Form W-2, Wage and Tax Statement. The TPA will also provide each civilian sponsor with the IRS Form 1099, Miscellaneous Income, at the end of each tax year.

Q. I don't receive a direct cash subsidy for my child's installation-based space. Why am I being assessed a subsidy value?

A. The cost of each space in DoD installation based child development programs is equally subsidized for both Military Service members and civilian patrons through appropriated funds. These subsidies include direct support for a limited number of staff salaries, equipment and supplies. Additional financial support is provided in the form of installation contracts, facility and grounds maintenance, and other personnel support. In the absence of subsidies, the cost of child development programs offered to both Military Service members and civilian employees would be significantly higher.

Q. How will I know the value of the child care subsidy for installation based programs?

A. Each civilian family will receive specific information about the subsidy value for the relevant tax year, beginning with tax year 2009. The information will be provided each year in a notice to all civilian patrons and will also appear on your Form W-2, Wage and Tax Statement.

Q. Does this apply only to civilian sponsors?

A. Yes. While there is no differentiation between civilian patrons and Service member patrons in regard to fee schedules or quality of care provided, there are distinctions in their treatment under the tax code. Section 134 of the Internal Revenue Code was amended by the Military Family Tax Relief Act providing an exclusion from taxes for benefits under dependent care assistance programs for active duty Service members. Efforts to include DoD civilian employees in this exclusion were not successful.

Q. How does the tax issue apply to retired military personnel who are not DoD employees but whose dependent children utilize CYS Child Care Programs?

A. Individuals are subject to a potential tax on child care subsidies on the basis of their enrollment in the child development system of care. For example, a parent/sponsor who enrolls their child on the basis of their civilian employment status, regardless of previous military service, is subject to the taxation and must report the subsidy. A parent/sponsor who enrolls their child on the basis of prior military service, as a retiree, is not subject to taxation.

Please note that civilian employees are granted a higher priority status for enrollment. A Service may allow retirees to enroll on a waiver/space available basis. Once enrolled, a parent/sponsor status cannot change their enrollment status to avoid the tax.

Q. What is the difference between an installation based child development program and a community based program?

A. For the purpose of the cost per space determination, installation based child development programs are defined as those programs that are located on property owned or leased by the federal government and programs supported by DoD installation personnel off the installation that are also funded by direct and indirect appropriated support.

A community based child development programs is defined as a program approved by the Under Secretary of Defense for Personnel and Readiness, USD (P&R), or the designated office, and located on non-government property.

Q. My child attends a community based child care program. How will I be affected?

A. The cash value of the subsidy paid to the community based child care provider on your behalf by your DoD employing organization, will be reported to a Third Party Administrator (TPA) who will maintain program information relevant to child care subsidies. The TPA will forward appropriate information to the Defense Finance and Accounting Service (DFAS) who in turn will report child care subsidies on your Form W-2, Wage and Tax Statement. The TPA will also provide each civilian sponsor with the IRS Form 1099, Miscellaneous Income, at the end of each tax year. This differs from installation child development programs where the value of the child care space, reported to the IRS, is impacted by both direct and indirect appropriated fund support.

Q. What is a DCAP?

A. A Dependent Care Assistance Plan (DCAP) is the formal document establishing the guidelines, requirements, and authority for subsidizing a portion of the cost of child care incurred by DoD civilian employees. The IRC allows exemptions on child care subsidies up to \$2,500 (for married individuals filing separately), or \$5,000 (for individuals filing as single, head of household, or married filing jointly), from gross income if the subsidies are made available through an employer Dependent Care Assistance Plan (DCAP).

To qualify for the exclusion, civilian employees must claim the child as a dependent on the employee's Federal income tax return. Additional guidance may be found in the Internal Revenue Service Publication 503 "Child and Dependent Care Expenses."

Q. I'm enrolled in a Dependent Care Flexible Spending Account (DCFSA). How does this affect me?

A. Civilian employees are also eligible to make pre-tax contributions up to \$5,000 in a Dependent Care Flexible Spending Account (DCFSA). Civilian employees enrolled in a DCFSA whose children receive care in a DoD child development program should note that DCFSA contributions are included in the \$5,000 (\$2,500 for married individuals filing separately) tax exempt amount. Thus the tax exempt \$2,500 or \$5,000 is an aggregate of the value of the subsidy of the care provided to children enrolled in DoD installation and community based child development programs, defined as programs approved by USD (P&R) or the designated office and located on non-government property, and the DCFSA contribution.

Here are some specific examples of how a family might be affected:

- A family received a subsidy of \$2,000 for the year for their child and withheld \$3,000 in their DCFSA, \$0 would be added to the W-2 because the family did not exceed the \$5,000 maximum amount allowed.
- A family received a subsidy of \$3,000 for the year and withheld \$3,000 in their DCFSA, \$1,000 would be added to the W-2.
- A family received a subsidy of \$2,000 for each of their 2 children (\$4,000 total subsidy) and withheld \$3k in their DCFSA, \$2,000 would be added to the W-2 ($\$2,000 + \$2,000 + \$3,000 - \$5,000 = \$2,000$).

Q. What if I have additional tax-related questions?

A. You may also wish to consult your tax advisor to ensure that you have calculated the child care credits and exemptions correctly. This memo is not intended to replace the specific advice of a tax expert.