THE CHILD AND DEPENDENT CARE TAX CREDIT (CDCTC)

What is the CDCTC?
The Child and Dependent Care Tax Credit (CDCTC) is a nonrefundable federal tax credit that helps families with the child and dependent care expenses they incur in order to work, look for work, or go to school. In 2017, the CDCTC was estimated to provide almost $3.5 billion in tax benefits to nearly 6.3 million families.¹ Today, over half the states, plus the District of Columbia, offer child and dependent care tax provisions that can be claimed in addition to the federal CDCTC (some of which are refundable).²

Families can claim up to $3,000 of out-of-pocket work-related child and dependent care expenses for one child or dependent, and up to $6,000 for two or more children or dependents.³ The amount of the CDCTC is calculated by applying a percentage, based on the family’s income, to the family’s care expenses. Families with Adjusted Gross Income (AGI) of $15,000 or less can claim a credit worth 35 percent of eligible expenses. The percentage decreases down to 20 percent for families with AGIs above $43,000. Families with two or more children or dependents are eligible for a maximum CDCTC of $2,100, and families with one child or dependent are eligible for a maximum credit of $1,050.⁴

The credit is nonrefundable, which means that the credit amount received by families cannot exceed the amount of taxes a family owes. For example, if a couple with two qualifying children qualifies for a CDCTC worth $1,120, but only has $50 in tax liability to apply against it, they could only receive a credit worth $50. Because families do not receive the excess credit amount as a refund, the federal CDCTC provides little or no benefit to low- and moderate-income working families.

Helping Families with the High Cost of Child Care
For over 60 years, the tax code has recognized that many families incur child or dependent care expenses in order to work. High-quality child care is essential to enable parents to get and keep a job and to give children a strong start toward success in school and life. Many families struggle to meet the high cost of care: the average annual cost of full-time care for one child in 2017 ranged from nearly $3,000 to over $23,000, depending on the age of the child, the type of care, and where the family lives.⁵ In 2017, the median annual cost for full-day, adult dependent care services was $18,200.⁶ Accessing affordable child care can be especially difficult for women, who are often paid less than men, and who are more likely to work part-time jobs and raise children on their own. And because child care costs can consume a significant portion of mothers’ incomes, high child care costs may discourage women’s participation in the workforce.

Public investments can help families with the high cost of the care they need to work. One such investment is direct child care assistance to low- and moderate-income families through the federal Child Care and Development Block Grant (CCDBG). While direct child care assistance remains the most effective way to help families access child care, the CDCTC and related state provisions can provide some help to families.

Unfortunately, because the CDCTC is not refundable, low- and moderate-income families (who may have little or no federal tax liability) receive limited benefit from the credit. In 2018, almost 75 percent of the CDCTC’s benefits are estimated to go to families with AGIs above $75,000.⁷ Although the IRS does not collect data by race (or gender), recent research by PolicyLink,⁸ Prosperity Now and the Institute for Taxation and Economic Policy has found that families with higher incomes are overwhelmingly more likely to be White.⁹
The CDCTC’s expense limits, moreover, are significantly lower than the average annual costs of care. Further, the percentage of expenses used to calculate the credit is insufficient in light of the share of family budgets that care expenses can consume. In addition, the credit amounts decrease over time because the parameters of the credit are not indexed for inflation. Finally, families receive the credit only once a year, after filing their federal tax return, despite the fact that they incur child and dependent care expenses throughout the year.

Ways to Improve the CDCTC

Congress has not changed the CDCTC since 2001, and improvements are sorely needed. It is important to note that the 2017 Tax Cuts and Jobs Act did not contain any improvements to the CDCTC. In fact, following the 2017 tax law, low- and moderate-income families will receive even less benefit from the CDCTC than under prior law.

Making the CDCTC refundable would allow many low-income families to benefit more from the credit: two-thirds of the benefits of making the credit refundable would go to families with incomes of $30,000 or less. Policymakers should also consider increasing the percentage of expenses used to calculate the credit to better reflect the share of family budgets that care expenses can consume. The CDCTC’s expense limits, moreover, could be increased to be more consistent with the average annual costs of care. Indexing the parameters of the credit for inflation would ensure that the credit amounts do not decrease over time.

Because many states offer child and dependent care tax credits based on the CDCTC, improvements to the federal credit would in many cases automatically boost the value of those state credits. Improving the CDCTC, especially if paired with a significant additional investment in the Child Care and Development Block Grant (CCDBG), would help more working families afford the care they need.

Resources:


3 Ibid, 4.
5 Sarah Hassmer and Amy Matsui, 2.
6 Ibid.
7 National Women’s Law Center, Improving the Child and Dependent Care Tax Credit Would Help Working Families with the High Cost of Child Care (Washington, DC: National Women’s Law Center, 2018).