

Dependent Care Overview



A “DCAP” is a **dependent care assistance program** that is also an FSA. An employee can use a DCAP to be reimbursed for employment-related expenses that allow the employee and his or her spouse to be “gainfully employed.” Employment-related expenses apply only to certain individuals. Typical DCAP expenses are those incurred to have a babysitter or day-care provider take care of an employee's child (under the age of 13) while Mom and Dad are both working, or to take care of a spouse or other tax dependent who lives with the employee and is incapable of self-care.

Keys Requirements

- The expenses must be “**employment related**” and must be incurred during the coverage period
- Employees cannot be reimbursed for expenses for which they claim the dependent care tax credit.
- **Only expenses incurred during the coverage period may be reimbursed.** An expense is incurred when the dependent care services giving rise to the expense have been provided. For example, a payment for care to be provided during the month of September cannot be reimbursed until the month of September has ended. Participants usually are given the run-out period to request reimbursement for expenses incurred during that plan year.
- There must be **adequate substantiation of the employment-related expenses.** The administrator must obtain information from an independent third party describing the service or product, the date of the service or sale, and the amount. The participant must also certify that the expense was not reimbursed (and will not be reimbursed) from any other source. Many employers also require the caregiver's taxpayer identification number (the Social Security number, for an individual), which the employee must provide to the IRS. If an electronic payment card program is offered, it must be administered in accordance with IRS rules regarding such programs.
- DCAP participants are subject to the **use-or-lose rule.** This means that contributions made to the plan that are not used during one plan year generally cannot be carried over to the next plan year. See your employer’s Plan Requirements for details.

Maximum Amount

There is a statutory limit on the amount of expenses that can be paid pre-tax under a DCAP. The limit is calculated on a calendar-year basis and is equal to the smallest of the following amounts:

- **\$5,000** (if the employee is married and filing a joint return or is a single parent);
- **\$2,500** (if the employee is married but filing separately);
- the employee's earned income; or
- the spouse's earned income (if the employee is married at the end of the taxable year).

If a spouse is not gainfully employed because he or she is a full-time student or is incapable of self-care, then the spouse will be deemed to have an income of \$250 per month for one qualifying individual or \$500 per month for two or more qualifying individuals.

Potential Qualifying Expenses* and Examples Only

Day Camp (not overnight) * **Classes that are primarily educational in nature** * **“Hold the Spot fee”** (IRS grey area)
* **Kindergarten** (not a qualifying expense) * **Late Fees** (as long as the payment relates directly to the care of the child) *
Nanny (extent care is attributable to qualifying individual) * **Pre School / Nursery School** (and similar programs below
level of kindergarten) * **Paid to Relatives or Elder Care** (potential qualifying expense and see conditions)

* See also **IRS Publication 503 (Child and Dependent care Expenses)** Please contact **125Company** for further details

Eligible Employment-Related Expenses

Expenses are employment related if they satisfy two tests. First, the employee must incur the expense to allow the employee (and the employee's spouse) to work (i.e., to be “gainfully employed”). Second, the expenses must be for the care of one or more “qualifying individuals.”

Whether expenses are incurred to allow someone to be gainfully employed generally is determined on a daily basis (although there are limited exceptions for certain short, temporary absences from work and part-time employment). Expenses can also be reimbursed if they are incurred while someone is looking for work or in order to be self-employed. Generally, a married employee can only be reimbursed for expenses if his or her spouse is also working or looking for work. A spouse is also considered to be gainfully employed, however, for any month that he or she is a full-time student or is mentally or physically incapable of self-care.

The care provided must be for the individual's “well-being and protection.” Generally, amounts paid for education, food, and clothing are not expenses paid for care, but if an expense for care also covers other services that are “incidental to and inseparably a part of” the care, then the entire amount is considered to be for care. For example, bills from a day-care center that provides meals in addition to child care would be reimbursable if the cost of the food could not be separated from the cost of care.

Expenses must be for the care of a qualifying individual. Generally, a qualifying individual is either (a) a child of the employee who is under age 13 and is the employee's tax dependent; or (b) a spouse or tax dependent who is physically or mentally incapable of self-care. A qualifying individual must have the same principal place of abode as the employee for more than half the year. A special rule for children of divorced or separated parents treats a child who is under age 13 or physically or mentally incapable of self-care as a qualifying individual with respect to the custodial parent when the noncustodial parent has the dependency exemption.

Some expenses are not reimbursable. For example, expenses for services provided outside an employee's home by a dependent care center that does not comply with applicable state and local law cannot be reimbursed. A plan may not reimburse dependent care payments made to (a) an employee's child who is under age 19; (b) someone for whom the employee (or the employee's spouse) can claim a dependency exemption; (c) the employee's spouse; or (d) the child's parent (if the child is under age 13). And payments for care outside the employee's household of a qualifying individual who is incapable of self-care (other than a child of the employee who is under age 13) generally cannot be reimbursed unless the qualifying individual regularly spends at least eight hours each day in the employee's household. Reference: EBIA 2015