



## Understanding the Taxation of NC State “WolfPup” Childcare Program

### TAX LIMITS

The Internal Revenue Service (IRS) limits employer-provided, tax-free childcare benefits to \$5,000 per family per year. If you file your taxes as “Married Filing Separately,” you and your spouse may each claim \$2,500. NC State University provides three types of pre-tax childcare benefits, all of which are subject to the \$5,000 total:

1. A **Tuition Reduction** subsidy for eligible program participants, based on family income;
2. A voluntary **Dependent Care Flexible Spending Account** (FSA) program allows employees to be reimbursed with pre-tax payroll contributions for qualified child and/or dependent adult care expenses. Because the money is deducted from your pay before taxes are calculated, and because it's not taxed when it is reimbursed, this money becomes tax-free income. For example, if someone would otherwise pay 30% in taxes (including federal income and FICA taxes) but they contribute \$5,000 a year to a dependent care FSA, they could possibly avoid paying \$1,500 in taxes.

The \$5,000 annual maximum includes all sources, such as a previous employer within the same calendar year or the employer of your child's other parent. The \$5,000 is a per-family (not per-child) maximum.

### HOW & WHY DO WOLFPUP SUBSIDIES COUNT TOWARD THE \$5,000 LIMIT?

You might think that Bright Horizons (BH) is cutting its fees and simply charging less to NC State employees. This is not the case. BH wouldn't have sufficient revenue to provide the excellent level of care it offers if it didn't charge full price. Instead, **NC State University pays the difference** in the cost of tuition for each child.

Family Income	BH Monthly Rates	NCSU Subsidy @ NCSU Center	Participants @ NCSU Center will Pay	Monthly Subsidy by NC State for Participants	Annualized Subsidy by NC State for Participants
<b>INFANTS</b>					
\$70,000+	\$1,555	11%	\$1,384	\$ 171	\$ 2,052
< \$70,000	\$1,555	31%	\$1,073	\$ 482	\$ 5,784
<b>TODDLERS</b>					
\$70,000+	\$1,455	11%	\$1,295	\$160	\$ 1,920
< \$70,000	\$1,455	31%	\$1,004	\$ 451	\$ 5,412
<b>TWO'S</b>					
\$70,000+	\$1,290	11%	\$1,148	\$ 142	\$ 1,704
< \$70,000	\$1,290	31%	\$890	\$ 400	\$ 4,800
<b>PRE-SCHOOL</b>					
\$70,000+	\$ 1,125	11%	\$1,001	\$ 124	\$ 1,488
< \$70,000	\$ 1,125	31%	\$776	\$ 349	\$ 4,188

*NOTE: Discounts Apply to Full-Time and Part-time Care; however employees must be employed full-time.*

On the pricing chart above, the amount that NC State contributes on your behalf each month is shown in the last column. That's the difference between what BH charges and what you actually pay. The university does not give you that money directly as additional income because it would be taxed. Instead, NC State pays that money directly to BH on your behalf. Since that money is never considered *your* income, you are not taxed on it. However, the 11% and 31% subsidies (based on family income) are considered employer-provided tax-free childcare benefits [provided the total does not exceed the \$5,000 limit].

### **WHAT HAPPENS IF I EXCEED THE \$5,000 LIMIT?**

IRS regulations do not limit the level of childcare benefits you can receive. It only limits the amount you can receive TAX-FREE. Any childcare benefits in excess of \$5,000 will be assessed by all the applicable federal and state taxes. So if you get \$6,000 a year in childcare benefits, \$1,000 will be taxed. Assuming a 30% federal tax rate, that means that you will pay an additional \$300 in taxes. Of course, even with taxes, it's still a good deal – you're receiving a \$1,000 benefit for only \$300. The additional amount for which you are taxed is called "childcare imputed income."

### **HOW MUCH CAN I CONTRIBUTE TO THE Dependent Care Flexible Spending Account (FSA)?**

- First, consider how much **employer-provided benefit** you will receive through the **Tuition Reduction** subsidy -- Not how much YOU pay, but how much the *University contributes on your behalf*. Add that to any other child care benefits you will receive from another source in the year.
- If that figure is *LESS THAN \$5,000*, then the difference between that amount and \$5,000 is how much you can contribute to a FSA to avoid taxation.
- Divide that number by the number of months you will contribute to a DDCFSA (the remaining number of months in the tax year if you are enrolling mid-year) to determine how much you can contribute to a DDCFSA each month.

WolfPup Benefits (including <b>Tuition Reduction</b> )	+	Other Child Care Benefits	=	<b>Employer Provided Benefits</b>
IRS Limit \$5,000	-	<b>Employer Provided Benefits</b>	=	Annual Dependent Care Account Contribution Allowed
FSA Amount	/	Months remaining in the year	=	Monthly FSA contribution

For example, if your total annual employer-provided subsidies are \$3,444, the amount left over from subtracting \$3,444 from \$5,000 is \$1,556. You may elect to have \$1,556 (\$129.67/month) deducted in pre-tax dollars as your FSA deduction. Determining the right FSA contribution amount is crucial -- because once you enroll in the FSA, you cannot change or cancel your enrollment during the year (unless you have a legally-qualifying "status" change).

If you contribute too much -- more than the amount calculated by using the method above -- you will lose the tax advantages of participating in the FSA on that excess amount. In addition to not realizing additional tax savings, it may also make your tax situation more complicated.

### **WHAT IF MY WOLFPUP BENEFITS EXCEED \$5,000?**

Take the time to review and understand the advantages and tax consequences of the University's employer-provided childcare benefits. If you receive over \$5,000 in employer-sponsored childcare benefits, then you will be charged taxes on the amount in excess of the limit. On your paycheck, you will see an amount listed as "childcare imputed income," and taxes will be charged to you.

### **EXAMPLES**

*EXAMPLE 1: Infant Care, Family Income less than \$40,000*

- The full cost for infant care is \$1,555 per month
- The rate after the 31% **Tuition Reduction** is \$1,073 per month
- This gives you a total subsidy of \$482 off the \$1,555 monthly rate
- So you pay \$1,073 per month out-of-pocket
- Your \$482/mo subsidy for the first ten months of the year (January through October) equals \$4,820.
- In November, you cross over the \$5,000 limit, so only \$180 of November is tax-free.

- The remaining \$302 in the month of November is taxable.
- In December, your entire \$482 discount would be taxable since the discount is over the \$5,000 limit.
- You will pay taxes on \$784. (Hey! Taxes on \$784 are still better than *paying* all \$784!)

**EXAMPLE 2:** Two-Year-Old Care; Family Income over \$90,000

- The full cost for a two-year-old is \$1,290 per month
- The rate after the 11% **Tuition Reduction** is \$1,148 per month (your out-of-pocket)
- Therefore, your employer-provided benefit is \$142 per month, or \$1,704 per year
- You want to take advantage of the maximum, pre-tax FSA benefit. Since you're already receiving the equivalent of \$1,704 as a tuition reduction, you can direct the remaining \$3,296 (\$5,000 annual limit - \$1,704 tuition reduction) into to a pre-tax FSA to reimburse your out-of-pocket expenses

**EXAMPLE 3:** HIRED Mid-Year

- You are hired by NC State on July 1, and immediately place your pre-schooler in NC State's center, where the full cost is \$1,125/month
- Your family income is \$75,000, so you are eligible for the 11% **Tuition Reduction**.
- You will pay \$1,001/mo out-of-pocket for six months, or a total of \$6,006.00.
- Your total subsidy would be \$124 per month, or \$744 for the remaining 6 months of the year
- Prior to coming to NC State University, you did not contribute into a dependent care FSA or receive other employer-sponsored childcare benefits, so you are entitled to the full \$5,000 annual limit
- You can direct the remaining \$4,256 (\$5,000 maximum - \$744) to a pre-tax FSA to reimburse your out-of-pocket expenses.

**HOW DOES NC STATE UNIVERSITY REPORT CHILDCARE IMPUTED INCOME TAXES?**

Your childcare benefits will be tracked in the University's payroll system and reported on your W-2. (NC State cannot track childcare benefits that you receive from another source, such as your spouse's employer. You will need to factor any additional benefits you receive when you estimate your additional taxation, and report it properly when preparing your federal tax return.) You will be taxed on the childcare benefits you receive from NC State in excess of \$5,000 *only in the months during which you exceed that limit*. Please keep in mind that some paychecks during the year will have more taxes taken out than others. Be sure to anticipate that when you budget.

**FOR MORE INFORMATION & FORMS on NC STATE'S WOLFPUP CHILDCARE PROGRAM**

If you have questions about the tax implications of your child care benefits or how much you may contribute to a dependent care FSA, please contact your Benefits Consultant at:

[http://www.ncsu.edu/human\\_resources/benefits/consultant.php](http://www.ncsu.edu/human_resources/benefits/consultant.php) or call (919) 515-2151.