



## Credit Where Credit is Due

Lower Your Taxes or  
Increase Your Refund to  
Help Your Family

**Tax Year 2004**

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Do you know that if you have children or other dependents you may be eligible for tax benefits that could reduce the taxes you pay or increase your tax refund? This booklet is designed to inform you about four of these tax benefits in the federal income tax code: the Dependent Care Tax Credit, the Child Tax Credit, the Earned Income Tax Credit, and the Dependent Care Assistance Program. The information provided here can help you determine if you are eligible to receive the tax assistance these provisions offer for tax year 2004, give you an idea of the amount of tax assistance you can receive and how to claim it, and answer some other questions you may have about these tax benefits. This booklet is not intended to provide legal assistance but to help you understand these tax benefits and the assistance they provide.

If you are eligible for the Dependent Care Tax Credit, the Child Tax Credit and the Earned Income Tax Credit, you can claim benefits under all three provisions. Under some circumstances you may be able to claim the Dependent Care Tax Credit even if you also receive benefits through a Dependent Care Assistance Program, although it is usually in your best interest to determine which of these two provides the most benefit to you and participate in that one to the maximum extent possible. You can use these tax benefits to reduce the federal income taxes you pay. Even if your income is so low that you don't pay federal income taxes, you may be able to get a tax refund by claiming the refundable Earned Income Tax Credit and/or Child Tax Credit.



These credits could mean hundreds or thousands of dollars for your family.

**This booklet is organized in four sections:**

-  **The 2004 Dependent Care Tax Credit, Child Tax Credit, Earned Income Tax Credit, and Dependent Care Assistance Program at a glance;**
-  **Eligibility for these tax benefits;**
-  **Determining the value of these tax benefits; and**
-  **Information on how to claim these tax benefits and how to obtain more information about them and similar state tax benefits.**

## Tax Benefits At-A-Glance

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### Dependent Care Tax Credit (DCTC)

The Dependent Care Tax Credit provides tax assistance to families who pay for child or dependent care in order to work in paid employment. In 2004 it can be as much as \$1,050 for 2004 employment-related care for one qualifying child or dependent, and as much as \$2,100 for 2004 employment-related care for two or more qualifying children or dependents. In general, the amount of your DCTC depends on:

- ☞ your adjusted gross income (together with your spouse's adjusted gross income, if you are married);
- ☞ the number of children or dependents in care;
- ☞ the amount you paid for care;
- ☞ the extent to which you have federal income tax liability; and
- ☞ whether and to what extent you participated in a Dependent Care Assistance Program offered by your employer.

In general, the higher your child and dependent care expenses and the lower your income, the larger your DCTC will be.

Individuals and couples at all income levels are eligible for the DCTC, but if you owe no federal income taxes, you will not benefit from the DCTC. However, even if you owe only a small amount of federal income taxes, claiming the DCTC can increase the amount of any tax refund you may receive.

**In general, the higher your child and dependent care expenses and the lower your income, the larger your DCTC will be.**



The size of your CTC or EITC, unlike the DCTC, does not depend upon your incurring any particular expenses.






### Child Tax Credit (CTC)

The Child Tax Credit provides tax assistance to some families with children. In 2004 it can be as much as \$1,000 for each of your qualifying children if you are single and you had 2004 modified adjusted gross income of \$94,000 or less, or if you are married and you (together with your spouse) had 2004 modified adjusted gross income of \$129,000 or less.

If you don't owe federal income taxes or the amount of the CTC for which you are eligible is greater than the amount of federal income taxes you owe, you can receive a refund of some or all of the CTC for which you are eligible if you (together with your spouse, if you are married) have at least \$10,750 in earned income for 2004 or if you have three or more children.

### Earned Income Tax Credit (EITC)

The Earned Income Tax Credit provides tax assistance to some low- and moderate-income families and individuals who work in paid employment. In 2004 it can be as much as:

-  \$2,604 if you have one qualifying child and your 2004 earned income and adjusted gross income is \$30,338 or less (if you are single), or \$31,338 or less (together with your spouse's earned income and adjusted gross income, if you are married);
-  \$4,300 if you have two or more qualifying children and your 2004 earned income and adjusted gross income is \$34,458 or less (if you are single), or \$35,458 or less (together with your spouse's earned income and adjusted gross income, if you are married); and
-  \$390 if you have no qualifying children and you (or your spouse, if you are married) were at least age 25 but under age 65 at the end of 2004, and your 2004 earned income and adjusted gross income is \$11,490 or less (if you are single), or \$12,490 or less (together with your spouse's earned income and adjusted gross income, if you are married).

If you have a qualifying child, you can receive a portion of your EITC in advance—that is, in your paycheck each pay period—to help you meet your current expenses.

If you don't owe federal income taxes, or if the amount of the EITC for which you are eligible is greater than the amount of federal income taxes you owe, you can still receive a refund for the difference between the EITC for which you are eligible and the federal income taxes you owe.

### Dependent Care Assistance Program (DCAP)

Employers are permitted to provide eligible employees up to \$5,000 per year in tax-free child and dependent care benefits if the benefits are provided through a Dependent Care Assistance Program. Employees do not have to pay federal income taxes, employers do not have to pay employment taxes, and neither employers nor employees have to pay Social Security and Medicare taxes (also known as "payroll taxes") on benefits offered through a DCAP. Employees may not have to pay state income taxes on these benefits either. In general, the eligibility requirements and the type of care covered under a DCAP are the same as under the DCTC.

Dependent Care Assistance Program benefits may take several forms, including cash reimbursements, vouchers, and the provision of care in an outside child or dependent care facility or in an employer's own child or dependent care facility. These benefits may be fully funded by the employer without requiring any contribution from employees. Most commonly, however, an employer establishes a DCAP as a salary-reduction plan, whereby employees are permitted to set aside amounts from their annual salaries to cover their employment-related child and dependent care expenses. A participating employee's pay is reduced by the amount the employee designates (subject to the \$5,000 limitation and sometimes subject to an additional employer limitation), and this amount is returned to the employee in the form of a tax-free reimbursement for child and dependent care expenses. In effect, the assistance received by the employee is the amount of money saved by not paying taxes on the amount by which the employee's pay was reduced. Because most employers provide DCAP benefits funded solely by salary reduction, the illustrations in this booklet focus mostly on DCAP salary-reduction plans.



## Eligibility for these Tax Benefits

This section will help you determine if you can receive tax benefits from the DCTC, CTC, EITC or a DCAP by answering some commonly asked questions about eligibility, including questions about the relationship of the tax benefits to each other and to your eligibility for specific government programs.

*Who is a qualifying child or dependent for the purpose of claiming the DCTC or receiving DCAP benefits, and a qualifying child for the purpose of claiming the CTC or EITC?*

### For DCTC/DCAP

A qualifying child is a child under age 13 at the time care was provided who lived with you in 2004 and whom you can claim as a dependent on your 2004 tax return. A qualifying dependent is 1) a disabled individual (including a child older than 13 or a parent) who lived with you in 2004, is physically or mentally incapable of self-care, and whom you claim as a dependent on your 2004 tax return, or 2) a disabled spouse who lived with you in 2004 and is physically or mentally incapable of self-care.

### For CTC

A qualifying child is your child (grandchild, great grandchild, etc.) or stepchild who was under age 17 on December 31, 2004, is a U.S. citizen or resident alien, and is claimed by you as a dependent on your 2004 tax return. There are special rules for siblings, nieces and nephews, married, adopted and foster children, and children who were born or died in 2004.

**For EITC**

A qualifying child is your child (grandchild, great grandchild, etc.) or stepchild who lived with you in your main home in the U.S. for more than six months in 2004, and who on December 31, 2004 was under age 19, or under age 24 and a full-time student, or any age and permanently and totally disabled. There are special rules for siblings, nieces and nephews, married, adopted and foster children, children who were born or died in 2004, and for a child who is also the qualifying child of another person.

*How do I know if I can claim someone as a dependent on my 2004 tax return?*

You can claim as a dependent on your 2004 tax return an individual 1) for whom you (and/or your spouse, if you are married) provided more than half of the support for 2004; and 2) who is your (or your spouse's, if you are married) child (grandchild, great grandchild, etc.), stepchild, sibling, stepsibling, parent (grandparent, great grandparent, etc.), stepparent, niece, nephew, aunt or uncle, or any individual who lived with you during all of 2004. There are special rules for married, adopted and foster children. Generally, an individual must be a U.S. citizen or resident alien, or a resident of Mexico or Canada, for you to be able to claim that individual as a dependent.

There is a special dependency test for your child if you are divorced, legally separated, or lived apart from your spouse for the last six months of 2004. In this instance you can claim your child as a dependent even if you did not actually provide over half of the child's support in 2004 if: 1) you had custody of the child for a longer time in 2004 than your spouse or ex-spouse; 2) one or both of you provided over half of the child's support in 2004; 3) one or both of you had custody of the child for more than half of 2004; and 4) you did not sign Internal Revenue Service (IRS) Form 8332 or a similar statement agreeing not to claim the child as a dependent for 2004.

*If I am divorced or separated from my spouse and my ex-spouse claims our child as a dependent, but I have custody of our child, can I claim the DCTC or receive DCAP benefits for the care of our child, or claim the CTC or EITC for our child?*

**For DCTC/DCAP**

If your spouse or ex-spouse claims the child as a dependent because you as the custodial parent signed IRS Form 8332 or a similar statement agreeing not to claim the child as a dependent for 2004, you can claim the DCTC or receive DCAP benefits if you incurred qualifying care expenses for the child and all of the following conditions apply: 1) you were divorced, legally separated, or lived apart from your spouse for the last six months of 2004; 2) you had custody of the child for a longer time in 2004 than your spouse or ex-spouse; 3) one or both of you provided over half of the child's support in 2004; and 4) one or both of you had custody of the child for more than half of 2004.

**For CTC/EITC**

You must actually claim the child as a dependent in order to claim the CTC for the child, but you do not have to be able to claim the child as a dependent (or actually claim the child as a dependent), in order to claim the EITC for the child.

*What is included in income for the purpose of claiming the DCTC, CTC and EITC, or for receiving DCAP benefits?*

**For DCTC/DCAP**

Adjusted gross income is used to determine the amount of your DCTC. Earned income may be used to limit the amount of child and dependent care expenses that you can claim for the DCTC or the benefits you can receive through a DCAP.

**For CTC**

Modified adjusted gross income is used to determine your eligibility for the CTC. Earned income is used to determine your eligibility for and the amount of your CTC refund.

**For EITC**

Both earned income and adjusted gross income are used to determine your eligibility for and the amount of your EITC.

In general, adjusted gross income is gross income, minus certain allowable deductions. It includes wages, salaries and tips and net income from self-employment, as well as unemployment compensation, alimony and taxable interest received, but not child support payments received. Certain allowable deductions include student loan interest and alimony paid. For most people, modified adjusted gross income is the same as adjusted gross income. Earned income is defined differently for the DCTC and DCAP than it is for the EITC and CTC. Your tax forms will help you determine what is earned income for each of these tax benefits. If you set aside part of your salary in a DCAP, that amount is excluded from income so that you do not have to pay tax on it. Therefore, in determining your adjusted gross income, modified adjusted gross income, and earned income you should subtract from your salary any reduction that may occur because of your participation in a DCAP.

*What kind of care can I use to claim the DCTC or to receive benefits through a DCAP?*

Most types of child and dependent care—including in a center, a church, or a family or adult day care home, or by a neighbor or relative (except care provided by your spouse or dependent, or your child who was under the age of 19 on December 31, 2004)—qualify as long as you paid for the care and the care was necessary for you to work or look for work in paid employment. If you are married, both you and your spouse must have needed the care to work or look for work, or one spouse must have been a full-time student or incapable of self-care.

**Most types of child and dependent care qualify for the DCTC and DCAP as long as you paid for the care and the care was necessary for you to work or look for work in paid employment.**



The primary purpose of the care must be for a child or dependent's well-being and protection; accordingly, amounts paid to provide food, clothing or education are not considered care expenses unless the manner of providing the care is such that it includes expenses for other benefits that are, according to the IRS, "incident to and inseparably a part of the care." The IRS illustrates this rule by stating that "educational expenses incurred for a child in the first or higher grade level" are not considered care expenses but "the full amount paid to a nursery school" is considered a care expense even though the school also furnishes lunch and educational services. (The IRS also takes the position informally that kindergarten expenses are not expenses for the care of a child, but has issued no written guidance to this effect.) Expenses for after-school programs and day camps during school vacations are covered, but expenses for overnight camps are not.

In addition, if the care is provided in a place that provides care for more than six persons, the provider must meet all applicable state and local regulations. In the case of a dependent, the care must be for an individual who regularly spends at least eight hours a day in the home of the person claiming the DCTC or benefiting from a DCAP, so care in a residential care facility (such as a nursing home) for spouses or other individuals who are incapable of self-care is not eligible.

*Are there limits on the amount of child and dependent care expenses that I can claim for the DCTC or the benefits that I can receive through a DCAP?*

You may not claim more than \$3,000 in care expenses for one child or dependent or \$6,000 in care expenses for two or more children or dependents for the DCTC, or receive more than \$5,000 in benefits through a DCAP for 2004. (The amount of your DCAP benefits are also subject to any limitations that may be imposed by your employer, including limitations necessary to comply with the requirement that a DCAP not discriminate in favor of highly compensated employees.) In the case of both the DCTC and a DCAP, the care expenses you claim must be less than your 2004 earned



**Maximum child and dependent care expenses/benefits**

**\$3,000**

DCTC expenses for one child/dependent

**\$6,000**

DCTC expenses for two children/dependents

**\$5,000**

DCAP benefits

income. If you are married, the expenses you claim must be less than your 2004 earned income or your spouse's 2004 earned income, whichever is smaller. There are special rules for calculating the earned income of a spouse who is a full-time student or incapable of self-care.

*May I claim the DCTC if I receive benefits under a DCAP?*

In some cases you are allowed to both claim the DCTC and participate in a DCAP. For example, if you incurred more child and dependent care expenses than you received in DCAP benefits, you may be able to claim the DCTC for the difference. If all of your child and dependent care expenses are covered by benefits received through a DCAP, you cannot claim the DCTC. For the expenses you can claim through a DCAP, you should determine whether participating in a DCAP or claiming the DCTC will provide more tax benefits to you.

*Is it better for me to participate in a DCAP or claim the DCTC?*

Most people will receive more federal tax benefits from participating in a DCAP to the maximum extent possible than from claiming the DCTC. However, some low- and moderate-income families will receive more federal tax benefits from claiming the DCTC than from participating in a DCAP, and some low-income families may actually lose some federal tax benefits by participating in a DCAP.

**Most people will receive more federal tax benefits from participating in a DCAP to the maximum extent possible than from claiming the DCTC.**



*What happens if I spend less on child and dependent care than the amount of my salary reduction for child and dependent care expenses under a DCAP?*

In general, if you do not use the full amount that you designated for salary reduction at the beginning of the plan year for child or dependent care expenses over the course of the year, you will lose the right to receive the “leftover” money. This is sometimes referred to as the “use it or lose it” rule and means that it is important to be careful when designating the amount of salary reduction that you want.

*Will my CTC or EITC refund affect my eligibility to receive government benefits?*

Usually, no. The amount of your CTC and EITC refunds will generally not be used to determine if you are eligible for Medicaid, Supplemental Security Income (SSI), Food Stamps, or low-income housing, nor will they be used to determine how much you can receive from those programs, as long as you spend the refunds in the month they are received or in the following month. Your CTC refund also generally will not be used to determine if you are eligible for, or how much you will receive in, Temporary Assistance for Needy Families (TANF) benefits or other federally funded federal, state or local benefit programs, as long as you spend the refund in the month it is received or in the following month. Each state is permitted to develop its own rules on whether the EITC refund will be used to determine eligibility for and the amount of TANF benefits, so be sure to check with your state TANF agency for the EITC rules in your state.



EITC  
DCAP  
CTC  
DCTC

## Determining the Value of these Tax Benefits

This section shows you how to estimate how much you can get from the four tax benefits. These are only approximations; the actual amounts you can receive will depend on your individual circumstances.

*How much can I get through the EITC?*

The amount you can get through the EITC depends on your income, the number of qualifying children in your family, and whether you are single or married.

### Instructions for estimating the value of the EITC:

You can use Table 1 or Table 2 to get an idea of how much you can receive through the EITC for 2004. Use Table 1 if you are single. Use Table 2 if you are married. Read down the first column until you find the dollar amount closest to your earned income or adjusted gross income level (as directed in the footnotes to the tables). Then read across that row to the column that applies to the number of children in your family to find the approximate amount you can expect to receive from the EITC. Remember to subtract from your salary any reduction that may have occurred because of your participation in a DCAP.

**The CTC and EITC can be received as a refund if you have little or no tax liability.**



**TABLE 1**

Earned Income Tax Credit Amounts, Tax Year 2004  
SINGLE

Earned Income/ AGI	One qualifying child	Two or more qualifying children	No qualifying children
\$0	\$0	\$0	\$0
\$2,000	\$680	\$800	\$153
\$4,000	\$1,360	\$1,600	\$306
\$6,000	\$2,040	\$2,400	\$390
\$8,000	\$2,604	\$3,200	\$267
\$10,000	\$2,604	\$4,000	\$114
\$12,000	\$2,604	\$4,300	\$0
\$14,000	\$2,604	\$4,300	\$0
\$16,000	\$2,291	\$3,887	\$0
\$18,000	\$1,971	\$3,466	\$0
\$20,000	\$1,652	\$3,045	\$0
\$22,000	\$1,332	\$2,624	\$0
\$24,000	\$1,012	\$2,202	\$0
\$26,000	\$693	\$1,781	\$0
\$28,000	\$373	\$1,360	\$0
\$30,000	\$54	\$939	\$0
\$32,000	\$0	\$518	\$0
\$34,000	\$0	\$0	\$0

Use earned income if your adjusted gross income is less than \$14,040. Use adjusted gross income if your adjusted gross income is more than \$14,040.

**TABLE 2**

Earned Income Tax Credit Amounts, Tax Year 2004  
MARRIED

Earned Income/ AGI	One qualifying child	Two or more qualifying children	No qualifying children
\$0	\$0	\$0	\$0
\$2,000	\$680	\$800	\$153
\$4,000	\$1,360	\$1,600	\$306
\$6,000	\$2,040	\$3,000	\$390
\$8,000	\$2,604	\$3,200	\$343
\$10,000	\$2,604	\$4,000	\$190
\$12,000	\$2,604	\$4,300	\$37
\$14,000	\$2,604	\$4,300	\$0
\$16,000	\$2,451	\$4,098	\$0
\$18,000	\$2,131	\$3,677	\$0
\$20,000	\$1,811	\$3,255	\$0
\$22,000	\$1,492	\$2,834	\$0
\$24,000	\$1,172	\$2,413	\$0
\$26,000	\$853	\$1,992	\$0
\$28,000	\$533	\$1,571	\$0
\$30,000	\$213	\$1,149	\$0
\$32,000	\$0	\$728	\$0
\$34,000	\$0	\$307	\$0
\$36,000	\$0	\$0	\$0

Use earned income if your adjusted gross income (together with your spouse's adjusted gross income) is less than \$15,040. Use adjusted gross income if your adjusted gross income (together with your spouse's adjusted gross income) is more than \$15,040.

## Example

If you are single, you have two qualifying children, and you earned \$32,000 in 2004 and received \$2,000 in salary-reduction DCAP benefits in 2004, you would look in Table 1 at the

row for \$30,000 in adjusted gross income (\$32,000 salary - \$2,000 in DCAP salary reduction = \$30,000 adjusted gross income). You would receive \$939 from the EITC.

If your income level falls between two of the dollar amounts listed, you can see the dollar range in which your EITC benefits will fall by reading across the rows for the income levels just above and just below your own. If, for example, you are married, you have two qualifying children, and you together with your spouse earned \$11,000 and did not participate in a salary-reduction DCAP in 2004, your 2004 EITC would be between \$4,000 and \$4,300.

Note that if you received part of your EITC in advance during 2004, you will receive the difference between the total EITC for which you are eligible and the amount you received in advance when you file your 2004 tax return.

You may also be able to receive some state tax benefits by claiming state-level EITCs or similar benefits. The following states have EITCs based on the federal EITC (states with a refundable credit are in bold): **Colorado** (currently suspended due to budget reasons), the **District of Columbia**, **Illinois**, **Indiana**, Iowa, **Kansas**, Maine, **Maryland**, **Massachusetts**, **Minnesota**, **New Jersey**, **New York**, **Oklahoma**, Oregon, Rhode Island, **Vermont**, Virginia (takes effect in 2006), and **Wisconsin**.

## How much can I get through the CTC?

The amount you can get through the CTC depends on the number of qualifying children in your family, your income, and in some cases the extent to which you have tax liability. Unlike the DCTC and DCAP, which depend on whether you have child and dependent care expenses, the CTC is available without respect to whether you have incurred any particular expenses.

The CTC is \$1,000 per child for single individuals with 2004 modified adjusted gross income below \$75,000 and married couples with 2004 modified adjusted gross income below \$110,000. The CTC gradually decreases for individuals and couples with modified adjusted gross income above these amounts, until it reaches zero for single individuals with modified adjusted gross income above \$94,000 and married couples with modified adjusted gross income above \$129,000.

### Instructions for estimating the value of the CTC:

To determine how much you can receive from the CTC for 2004, multiply \$1,000 by the number of children you have. You will receive less than this amount if your 2004 modified adjusted gross income is above \$75,000 (if you are single) or above \$110,000 (together with your spouse's modified adjusted gross income, if you are married). Remember that your modified adjusted gross income may be lowered by participation in a DCAP.

## Example

If you are single, you have two qualifying children, and your earned income and modified adjusted gross income in 2004 was \$50,000 (after taking into account any reduction in

earned income and modified adjusted gross income because of participation in a DCAP), you would receive a 2004 CTC of \$2,000 (\$1,000 x 2).

Even if you pay little or no federal income taxes, you may be able to receive all or part of the CTC as a refund. Your tax forms walk you through the calculation. In brief, if all or some portion of the CTC is unused because the amount of your CTC exceeds the amount of taxes you owe, a further calculation is necessary to determine if you can receive all or part of the CTC as a refund.

#### Instructions for estimating a CTC refund:

Any refund you can receive for 2004 is equal to either 1) the unused portion of your CTC or 2) 15% of your 2004 earned income (together with your spouse's earned income, if you are married) over \$10,750, whichever is less. (Remember that your earned income may be lowered because of participation in a DCAP.) On the following page you will find the special rules for determining the CTC refund for families with three or more children.

#### Example

If you are single, you have two qualifying children and \$18,000 in 2004 earned income and modified adjusted gross income (after taking into account any reduction in earned income and modified adjusted gross income that may occur because of your participation in a DCAP), you would qualify for a maximum CTC of \$2,000, but you would have only \$155 in federal income tax liability. You would receive a CTC of \$155 to offset your

tax liability. Fifteen percent of your earned income above \$10,750 ( $\$18,000 - \$10,750 = \$7,250$ ) is \$1,088 ( $\$7,250 \times 15\%$ ). Since this amount is less than your unused CTC amount of \$1,845 ( $\$2,000$  maximum CTC -  $\$155$  CTC used to offset tax liability =  $\$1,845$ ), you would receive a CTC refund of \$1,088. In total, you would receive a 2004 CTC of \$1,243 ( $\$155$  to offset your tax liability and  $\$1,088$  as a refund).

#### Instructions for estimating a CTC refund for families with three or more children:

If you have three or more children, you can also calculate your refund according to a different formula. Under the alternate formula, you must first calculate the total amount of payroll taxes that have been withheld from your paycheck during the tax year. (In 2004, your payroll tax equals 7.65% of your first \$87,900 of earnings.) From this amount you must subtract the total amount of the EITC that you receive, including any portion of the EITC that you receive as a tax refund. You can receive as a CTC tax refund the amount by which the payroll taxes that you paid exceed the EITC that you receive, up to the full amount of the CTC for which you are eligible. If you have three or more children, you should calculate your CTC using both methods for determining the CTC refund and choose the one that provides a higher refund to you.

#### Example

If you are single, you have three children and \$30,000 in 2004 earned income and modified adjusted gross income (after taking into account any reduction in earned income and modified adjusted gross income that may occur because of your participation in a DCAP), you would qualify for a maximum CTC of \$3,000. You would have \$1,058 in tax liability and would receive a CTC of \$1,058 to offset this liability. You would qualify for an EITC of \$939 and pay \$2,295 in payroll taxes ( $\$30,000 \times 7.65\% = \$2,295$ ). Using the

payroll tax/EITC method for calculating the CTC refund, you would qualify for a CTC refund of either \$1,358 ( $\$2,295$  in payroll taxes -  $\$939$  in EITC =  $\$1,358$ ) or \$1,942 (the unused amount of the CTC,  $\$3,000 - \$1,058 = \$1,942$ ), whichever is lower. Using the 15% method, you would qualify for a CTC refund of \$2,888 (15% of earned income above \$10,750) or \$1,942 (the unused amount of the CTC), whichever is lower. The 15% method provides you with a higher refund. You would receive a CTC refund of \$1,942.

Note: The instructions for your tax return walk you through each of these calculations.

### How much can I get through the DCTC?

The amount you can get through the DCTC depends on your adjusted gross income, the number of qualifying children or dependents in care, the amount you paid for care, and the extent to which you have federal income tax liability. It also depends on whether and to what extent you participated in a DCAP.

The DCTC is calculated as a percentage of qualifying child and dependent care expenses. Qualifying expenses for 2004 may not exceed \$3,000 for one child or dependent and \$6,000 for two or more children or dependents. Individuals and couples with 2004 adjusted gross incomes of \$15,000 or less receive a credit equal to 35 percent of eligible expenses, for a maximum of \$2,100. The rate decreases as adjusted gross income increases above \$15,000 until it reaches 20 percent for individuals and couples with adjusted gross incomes above \$43,000.

#### Instructions for estimating the value of the DCTC:

The following table gives you a general idea of how much the 2004 DCTC is worth to you by showing the amount of the DCTC available for individuals and couples at different income levels with varying child or dependent care expenses. To determine the amount of the DCTC you can expect to receive, look down the first column of Table 3 to find the dollar range in which your 2004 adjusted gross income falls. Then read across that row to the column that most closely matches the amount you spent on child or dependent care during 2004 to find the DCTC you can expect to receive. Note that if you have one child or dependent, you may claim no more than \$3,000 in expenses.

### TABLE 3

Sample Child and Dependent Care Tax Credit Amounts for Tax Year 2004

Adjusted Gross Income	Care Expenses for One or More Qualifying Children or Dependents*			Care Expenses for Two or More Qualifying Children or Dependents		
	\$1,000	\$2,000	\$3,000	\$4,000	\$5,000	\$6,000+
\$0-\$15,000	\$350	\$700	\$1,050	\$1,400	\$1,750	\$2,100
\$15,001-\$17,000	\$340	\$680	\$1,020	\$1,360	\$1,700	\$2,040
\$17,001-\$19,000	\$330	\$660	\$990	\$1,320	\$1,650	\$1,980
\$19,001-\$21,000	\$320	\$640	\$960	\$1,280	\$1,600	\$1,920
\$21,001-\$23,000	\$310	\$620	\$930	\$1,240	\$1,550	\$1,860
\$23,001-\$25,000	\$300	\$600	\$900	\$1,200	\$1,500	\$1,800
\$25,001-\$27,000	\$290	\$580	\$870	\$1,160	\$1,450	\$1,740
\$27,001-\$29,000	\$280	\$560	\$840	\$1,120	\$1,400	\$1,680
\$29,001-\$31,000	\$270	\$540	\$810	\$1,080	\$1,350	\$1,620
\$31,001-\$33,000	\$260	\$520	\$780	\$1,040	\$1,300	\$1,560
\$33,001-\$35,000	\$250	\$500	\$750	\$1,000	\$1,250	\$1,500
\$35,001-\$37,000	\$240	\$480	\$720	\$960	\$1,200	\$1,440
\$37,001-\$39,000	\$230	\$460	\$690	\$920	\$1,150	\$1,380
\$39,001-\$41,000	\$220	\$440	\$660	\$880	\$1,100	\$1,320
\$41,001-\$43,000	\$210	\$420	\$630	\$840	\$1,050	\$1,260
\$43,001+	\$200	\$400	\$600	\$800	\$1,000	\$1,200

\* Individuals or couples with only one qualifying child or dependent may claim no more than \$3,000 in qualifying expenses.

## Example

If your 2004 adjusted gross income was \$55,000, you have two qualifying children, and you spent \$5,000 on work-related child care in 2004, you would look in Table 3 at the row for \$43,000+ in adjusted gross income. You would receive \$1,000 in 2004 federal tax savings from the DCTC.

You may find that the exact amount you spent on child or dependent care is not listed. If this is the case, the table will provide you with the dollar range in which your DCTC will fall. Find your 2004 adjusted gross income level in the first column of the table and read across to the columns just below and just above the amount you spent. Your DCTC will fall between the two amounts listed. If, for example, your 2004 adjusted gross income was \$55,000, you have two qualifying children, and you spent \$4,500 on work-related child care in 2004, you would receive between \$800 and \$1,000 in 2004 federal tax savings from the DCTC.

If your employer offers a DCAP and you participated in that program in 2004, your calculation of the DCTC will be affected in two ways. First, to determine your adjusted gross income you must subtract from your salary any reduction that may have occurred because of your participation in a DCAP. Second, you must subtract the amount of any DCAP benefits you receive from the maximum expense limits for the DCTC to determine the new maximum amount of expenses you can claim for the DCTC. You must then compare your qualifying expenses (over and above what you received in DCAP benefits) to this new maximum amount to determine the actual amount of expenses you can claim for the DCTC.

## Example

If you earned \$40,000 in 2004, you have one qualifying child, you spent \$2,500 on work-related child care in 2004, and you set aside \$1,500 in a DCAP, your adjusted gross income would be \$38,500 (\$40,000 salary - \$1,500 in DCAP salary reduction = \$38,500 adjusted gross income). The new maximum amount of expenses you can claim for the DCTC would be \$1,500 (\$3,000 DCTC expense limit -

\$1,500 DCAP benefit = \$1,500). You have \$1,000 in expenses over and above what you received in DCAP benefits, and this amount is less than your new maximum amount of expenses for the DCTC, so you could claim the DCTC for \$1,000 in expenses. You would look in Table 3 at the row for \$37,001-\$39,000 in adjusted gross income. You would receive \$230 in 2004 federal tax savings from the DCTC.

If you have no tax liability you are not able to benefit from the DCTC, and if your tax liability is low, you may not be able to benefit from the full amount of the DCTC for which you are otherwise eligible. This is because the DCTC, unlike the CTC and the EITC, is not refundable.

You may also be able to receive some state tax benefits by claiming state-level child and dependent care tax provisions. The following states have such provisions (states with refundable provisions are in bold: **Arkansas**, **California**, **Colorado**, Delaware, the District of Columbia, **Hawaii**, Idaho, **Iowa**, Kansas, Kentucky, **Louisiana**, **Maine**, Maryland, Massachusetts, **Minnesota**, Montana, **Nebraska**, **New Mexico**, **New York**, North Carolina, Ohio, Oklahoma, **Oregon**, Rhode Island, South Carolina, **Vermont**, and Virginia.

*How much can I get through a DCAP?*

The amount of federal tax savings you can receive by participating in a DCAP depends on the amount of DCAP benefits your employer provides (whether through salary reduction or otherwise) and your marginal tax rates, since you do not pay taxes on these benefits. Your marginal tax rates are the tax rates you pay on your last dollar of income. The amount of your federal tax savings also depends on the extent to which you have tax liability.

If you have no tax liability and do not receive the 2004 EITC, you will receive no federal income tax savings from participating in a DCAP. If your tax liability is low and you do not receive the 2004 EITC, you may not be able to benefit fully from the tax savings otherwise available through a DCAP. If you receive the 2004 EITC, the value to you of participating in a DCAP will depend not only on your tax liability, but also on the effect of your DCAP participation on the size of your 2004 EITC. Participating in a DCAP lowers the amount of your earnings that are used to calculate the EITC, which can either raise or lower the amount of your EITC.

To determine the amount of your tax savings, you must first determine your marginal income and payroll tax rates.

**Instructions for estimating federal marginal income tax rate for non-EITC recipients:**

If you do not receive the 2004 EITC, determining your 2004 federal marginal income tax rate is relatively simple. Tables 4 and 5 give you a general idea of the federal marginal income tax rates for 2004 for families who do not receive the 2004 EITC. Use Table 4 if you are single. Use Table 5 if you are married. To estimate your federal marginal income tax rate if you do not receive the 2004 EITC, follow the instructions accompanying either Table 4 or Table 5, as appropriate, and read down the first two columns to find the dollar range in which your 2004 adjusted gross income falls. (Remember to take into account any reduction in salary that may have occurred because of your participation in a DCAP.) Then read across that row to find your 2004 marginal income tax rate.

**The amount of federal tax savings you can receive by participating in a DCAP depends on the amount of DCAP benefits your employer provides (whether through salary reduction or otherwise) and your marginal tax rates, since you do not pay taxes on these benefits.**



**E x a m p l e**

If you are married, you have two qualifying children, and you (together with your spouse) had adjusted gross income of \$50,000 (after subtracting from your salary any reduction that may have occurred because of your participation in a DCAP) in 2004, you would look in Table 5. Following the

instructions in the table, since you have more than one qualifying child you would add \$3,100 to each of the income levels listed. The relevant income range for you would be \$36,400 to \$80,200. You would have a 2004 federal marginal income tax rate of 15 percent.

**TABLE 4**

Approximate Federal Marginal Income Tax Rates for 2004 for Single Individuals Who Do Not Receive the 2004 EITC

If your adjusted gross income is greater than...	But less than...	Your marginal income tax rate is...
0	\$23,550	10%
\$23,550	\$52,250	15%
\$52,250	\$113,850	25%
\$113,850	\$176,050	28%
\$176,050	\$319,100	33%
\$319,100		35%

This table assumes that eligible tax filers claim the standard deduction for head of household filers, the personal exemption, and a dependent exemption for one child or dependent. You should add \$3,100 to each income level for each additional child or dependent for whom you claim a dependent exemption if your adjusted gross income is below \$178,350. If 1) your adjusted gross income is above this amount and you have more than one child or dependent, or 2) any of the other assumptions do not apply to your situation, this table will not accurately reflect your marginal tax rate.

**TABLE 5**

Approximate Federal Marginal Income Tax Rates for 2004 for Married Couples Who Do Not Receive the 2004 EITC

If your and your spouse's adjusted gross income is greater than...	But less than...	Your marginal income tax rate is...
0	\$33,300	10%
\$33,300	\$77,100	15%
\$77,100	\$136,250	25%
\$136,250	\$197,650	28%
\$197,650	\$329,358	33%
\$329,358		35%

This table assumes that eligible tax filers claim the standard deduction for married couples filing jointly, the personal exemption for the tax filer and the tax filer's spouse, and a dependent exemption for one child or dependent. You should add \$3,100 to each income level for each additional child or dependent for whom you claim a dependent exemption if your adjusted gross income (together with your spouse's adjusted gross income) is below \$214,050. If 1) your adjusted gross income is above this amount and you have more than one child or dependent, or 2) any of the other assumptions do not apply to your situation, this table will not accurately reflect your marginal tax rate.

**Instructions for estimating federal marginal income tax rate for EITC recipients:**

If you receive the 2004 EITC, determining your 2004 federal marginal income tax rate is more complicated. The amount of your EITC can change as your income changes. Because it is difficult to simplify this calculation for some families, only a range of federal marginal income tax rates is provided here. If you receive the 2004 EITC for families without a qualifying child and your 2004 adjusted gross income is above \$6,390, if you are single, or \$7,390 (together with your spouse’s adjusted gross income), if you are married, your 2004 federal marginal income tax rate is 17.65 percent. If you receive the 2004 EITC for families with a qualifying child and your 2004 adjusted gross income is above \$14,040, if you are single, or \$15,040 (together with your spouse’s adjusted gross income), if you are married, your 2004 federal marginal income tax rate ranges from 26 percent to 36 percent. (If you receive the 2004 EITC and your 2004 adjusted gross income is below the amounts listed above for your situation, you will usually receive little or no federal tax savings—and may actually lose some federal EITC benefits—from participating in a DCAP.) Remember in determining your adjusted gross income to take into account any reduction in salary that may have occurred because of your participation in a DCAP.

**Instructions for estimating federal marginal payroll tax rate:**

Table 6 gives you a general idea of the federal marginal payroll tax rates for 2004. To estimate your federal marginal payroll tax rate, read down the first two columns of Table 6 and find the dollar range in which your 2004 earnings fall, remembering to take into account any reduction in earnings that may have occurred because of your participation in a DCAP. Then read across that row to find your 2004 federal marginal payroll tax rate. Note that for the purpose of calculating the payroll tax savings from participating in a DCAP for married couples, the relevant federal marginal payroll tax rate depends on the earnings of the spouse who participated in a DCAP offered by his or her employer, not on the combined earnings of the couple. In all the examples of married couples in this booklet, both spouses have the same marginal payroll tax rate since their combined earnings are below \$87,900. Therefore, it does not matter which spouse participated in the DCAP and the examples do not differentiate between the earnings of the husband and the earnings of the wife to determine the relevant federal marginal payroll tax rate.

TABLE 6

Federal Marginal Payroll Tax Rates for 2004

If your earnings are greater than...	But less than...	Your marginal payroll tax rate is...
0	\$87,900	7.65%
\$87,900		1.45%

The federal payroll tax assessed on employees is 7.65% of earnings below \$87,900 and 1.45% of earnings above \$87,900. If you have earnings from self-employment, this table will not accurately reflect your federal marginal payroll tax rate.

## Example

If you earned \$50,000 in 2004 (after taking into account any reduction in salary that may have occurred because of participation in a DCAP), you would

look in Table 6 at the row for between \$0 and \$87,900 in earnings. Your 2004 federal marginal payroll tax rate would be 7.65 percent.

### Instructions for estimating federal tax savings from participating in DCAP:

You can estimate your federal tax savings from participating in a DCAP by multiplying the amount of DCAP benefits your employer provides by your federal marginal tax rates and adding together the federal income and payroll tax savings.

## Example

If you do not receive the 2004 EITC, you are married and you (together with your spouse) earned \$50,000 in 2004 (after subtracting from your earnings any reduction that may have occurred because of your participation in a DCAP), your federal marginal income tax rate would be 15 percent and your federal marginal payroll tax rate would be 7.65 percent (since you and your spouse have combined earnings of less

than \$87,900, your federal marginal payroll tax rate is the same regardless of which spouse participated in the DCAP). If you have \$5,000 in DCAP benefits in 2004, you would receive \$750 ( $\$5,000 \times 15\%$ ) in federal income tax savings and \$383 ( $\$5,000 \times 7.65\%$ ) in federal payroll tax savings. Adding these figures together gives you a rough estimate of your 2004 federal tax savings—\$1,133—from participating in a DCAP.

## Example

If you receive the 2004 EITC for families with a qualifying child and your 2004 adjusted gross income (after subtracting from your salary any reduction that may have occurred because of your participation in a DCAP) is above \$14,040, if you are single, or \$15,040 (together with your spouse's adjusted gross income), if you are married, you have a federal marginal income tax rate of between 26 and 36 percent and a federal

marginal payroll tax rate of 7.65 percent. If you have \$5,000 in DCAP benefits, you would receive between \$1,300 and \$1,800 ( $\$5,000 \times 26\% = \$1,300$  and  $\$5,000 \times 36\% = \$1,800$ ) in federal income tax savings and \$383 ( $\$5,000 \times 7.65\%$ ) in federal payroll tax savings. Adding these figures together gives you a rough estimate of your 2004 federal tax savings—between \$1,683 and \$2,183—from participating in a DCAP.

It is important to remember that when you set aside part of your salary in a DCAP, you reduce the amount of earnings credited to you for the purpose of determining the amount of your Social Security benefits. Although this could have some effect on the Social Security benefits you receive in the future, for most individuals the effect is very modest.

You may also receive some state tax savings from participating in a DCAP; the amount you save will depend on your state marginal tax rate.

If your employer offers DCAP benefits that are not funded by salary reduction, you need to add the tax savings you receive from participating in the DCAP to the amount of DCAP benefits your employer provides you over and above your full salary to determine the total value to you of participating in the DCAP.

## Example

If you do not receive the 2004 EITC, you are married, and you (together with your spouse) earned \$55,000 and received \$5,000 over and above your salary in DCAP benefits in 2004, your federal marginal income tax rate (calculated on \$55,000) would be 15 percent and your federal marginal payroll tax rate would be 7.65 percent. You would receive \$750 ( $\$5,000 \times$




15%) in federal income tax savings and \$383 ( $\$5,000 \times 7.65\%$ ) in federal payroll tax savings from participating in a DCAP. Adding these figures together gives you a rough estimate of your 2004 federal tax savings—\$1,133—from participating in a DCAP. The total value to you of participating in this DCAP is \$6,133 ( $\$5,000 + \$1,133$  in federal tax savings).

Note that participating in a DCAP may also affect the amount of the CTC you may receive. If your 2004 modified adjusted gross income is above the maximum income level eligible for the CTC (\$94,000 (if you are single) or \$129,000 (together with your spouse's modified adjusted gross income, if you are married)), participating in a DCAP may reduce your modified adjusted gross income below that maximum threshold, making you eligible for the CTC. If your 2004 earned income is at least \$10,750 and below \$31,000, participating in a DCAP may affect the size of the CTC you receive. Because it is impossible to generalize about the magnitude of these effects, they are not included in the calculations for estimating the value of participating in a DCAP described above. But the following section provides some general guidelines about whether claiming the DCTC or participating in a DCAP is likely to be more beneficial, including for families eligible for the CTC.

## Is it more beneficial for me to participate in a DCAP or claim the DCTC?

Most people—particularly families with more than \$40,000 in adjusted gross income (before any reduction that may occur because of participation in a DCAP)—will receive more federal tax savings from participating in a DCAP to the maximum extent possible than from claiming the DCTC.

However, some single individuals and married couples with adjusted gross income below \$40,000 (before any reduction that may occur because of participation in a DCAP) may receive more tax savings from claiming the DCTC. Whether these individuals and couples receive more federal tax savings from participating in a DCAP or claiming the DCTC depends on their income level, whether they receive the EITC and CTC, their family composition, their marital status, and the amount of their child and dependent care expenses.

-  If your adjusted gross income for 2004 (together with your spouse's adjusted gross income, if you are married) before taking into account any reduction that may occur because of your participation in a DCAP is below \$15,000 (if you are single) or below \$16,000 (together with your spouse's adjusted gross income, if you are married) and you claim the EITC for families with a qualifying child and the CTC in 2004, you will usually receive more 2004 federal tax savings from claiming the DCTC than from participating in a DCAP. In fact, you may actually lose federal tax benefits by participating in a DCAP.
-  If your adjusted gross income for 2004 (together with your spouse's adjusted gross income, if you are married) before taking into account any reduction that may occur because of your participation in a DCAP is between \$32,000 and \$40,000, you claim the CTC in 2004, and you claim the EITC for families with a qualifying child in 2004 or would claim it if participating in a DCAP would reduce your adjusted gross income enough to make you income-eligible for the EITC, you may receive more 2004 federal tax savings from claiming the DCTC than from participating in a DCAP. Tables 7 and 8 will help you figure out whether participating in a DCAP or claiming the DCTC is more advantageous for you. Use Table 7 if you have one qualifying child. Use Table 8 if you have two qualifying children.
-  If your adjusted gross income for 2004 (together with your spouse's adjusted gross income, if you are married) before taking into account any reduction that may occur because of your participation in a DCAP is below \$40,000 and you do not claim the EITC for families with a qualifying child and the CTC in 2004, you may receive more 2004 federal tax savings from claiming the DCTC than from participating in a DCAP. You should do the calculations described earlier in this booklet to determine whether claiming the DCTC or participating in a DCAP is more advantageous for you.

Remember when calculating your tax savings that the value to you of claiming the DCTC or participating in a DCAP could be limited by your tax liability.

## Example

If you are single, you have one qualifying child, and you have \$35,000 in adjusted gross income (before taking into account any salary reduction that may occur because of your participation in a DCAP) and \$3,000 in child care expenses in 2004, you are within the exception for adjusted gross income in the \$32,000 - \$40,000 range if you

claim the CTC (you are not income-eligible for the EITC). Table 7 shows that you will receive more 2004 federal tax savings from claiming the DCTC than from participating in a DCAP. You will receive \$750 in 2004 federal tax savings from claiming the DCTC or \$680 in 2004 federal tax savings from participating in a DCAP.

If you have child or dependent care expenses in excess of what you are allowed to claim through a DCAP (either because of the \$5,000 limit imposed by law or a limit set by your employer), you should claim the DCTC for those expenses (up to the amount of the DCTC expense limit).

## Example

If you are married, you have two qualifying children, and you (together with your spouse) have \$55,000 in adjusted gross income (before taking into account any reduction that may occur because of your participation in a DCAP) and \$7,000 in child care expenses, you will receive more 2004 federal tax savings from participating in a DCAP to the maximum extent possible than from claiming the DCTC for those expenses. However, because you can only receive \$5,000 in DCAP

benefits and you have an additional \$2,000 in child care expenses, you can also claim the DCTC. Subtracting the \$5,000 you will receive in DCAP benefits from the \$6,000 DCTC expense limit gives you a new DCTC expense limit of \$1,000. You can claim the DCTC for \$1,000 of your remaining \$2,000 in child care expenses. You will receive \$200 in 2004 tax savings from the DCTC and \$1,133 in 2004 tax savings from the DCAP. Your total 2004 federal tax savings will be \$1,333.

**Is the DCAP or DCTC Better for Families with One Qualifying Child and Adjusted Gross Incomes Between \$32,000 and \$40,000?**

TABLE 7

Single Parent with One Qualifying Child

Adjusted Gross Income	Child or Dependent Care Expenses					
	\$1,000	\$2,000	\$3,000	\$4,000	\$5,000	\$6,000+
\$32,000	DCTC	DCTC	DCAP	DCAP	DCAP	DCAP
\$33-\$39,000	DCTC	DCTC	DCTC	DCAP	DCAP	DCAP
\$40,000	DCAP	DCAP	DCAP	DCAP	DCAP	DCAP

Married Couple with One Qualifying Child

Adjusted Gross Income	Child or Dependent Care Expenses					
	\$1,000	\$2,000	\$3,000	\$4,000	\$5,000	\$6,000+
\$32,000	DCTC	DCAP	DCAP	DCAP	DCAP	DCAP
\$33-\$39,000	DCTC	DCTC	DCTC	DCAP	DCAP	DCAP
\$40,000	DCAP	DCAP	DCAP	DCAP	DCAP	DCAP

This table assumes that single parents file as head of household, that married couples file as married filing jointly, and that the parents claim exemptions for themselves and claim the dependent exemption, the EITC and the CTC for only one qualifying children if income-eligible.

**Is the DCAP or DCTC Better for Families with Two Qualifying Children and Adjusted Gross Incomes Between \$32,000 and \$40,000?**

TABLE 8

Single Parent with Two Qualifying Children

Adjusted Gross Income	Child or Dependent Care Expenses					
	\$1,000	\$2,000	\$3,000	\$4,000	\$5,000	\$6,000+
\$32-\$35,000	DCAP	DCAP	DCAP	DCAP	DCAP	DCAP
\$36,000	DCTC	DCAP	DCAP	DCAP	DCAP	DCAP
\$37,000	DCTC	DCTC	DCAP	DCAP	DCAP	DCAP
\$38,000	DCTC	DCTC	DCTC	DCAP	DCAP	DCAP
\$39,000	DCTC	DCTC	DCTC	DCTC	DCAP	DCAP
\$40,000	DCAP	DCAP	DCAP	DCAP	DCAP	DCAP

Married Couple with Two Qualifying Children

Adjusted Gross Income	Child or Dependent Care Expenses					
	\$1,000	\$2,000	\$3,000	\$4,000	\$5,000	\$6,000+
\$32-\$36,000	DCAP	DCAP	DCAP	DCAP	DCAP	DCAP
\$37,000	DCTC	DCTC	DCAP	DCAP	DCAP	DCAP
\$38,000	DCTC	DCTC	DCAP	DCAP	DCAP	DCAP
\$39,000	DCTC	DCTC	DCTC	DCAP	DCAP	DCAP
\$40,000	DCAP	DCAP	DCAP	DCAP	DCAP	DCAP

This table assumes that single parents file as head of household, that married couples file as married filing jointly, and that the parents claim exemptions for themselves and claim the dependent exemption, the EITC and the CTC for only two qualifying children if income-eligible.

If you have determined that you will receive more 2004 federal tax savings from participating in a DCAP than from claiming the DCTC, you should also consider the effect of this participation on your state taxes. In general, you will receive more combined federal and state tax savings from participating in a DCAP than from claiming the federal DCTC and your state child and dependent care tax provision. In some cases, however, participating in a salary-reduction DCAP may adversely affect your eligibility for and the amount you can receive from a state child and dependent care tax provision. Especially if you live in California, Minnesota, Nebraska, New York, or Oregon, you should try to weigh the effect on your state taxes before deciding to participate in a salary-reduction DCAP; you may be better off claiming the federal DCTC and your state child and dependent care tax provision than participating in a salary-reduction DCAP.

As described above, if your employer offers DCAP benefits that are not funded by salary reduction, you need to add the tax savings you receive from participating in the DCAP to the amount of DCAP benefits your employer provides you over and above your full salary to determine the total value to you of participating in a DCAP. For most people whose DCAP benefits are not funded by salary reduction, the total value of participating in a DCAP will be greater than the tax savings from claiming the DCTC. However, if your DCAP benefits are partially funded by your employer and partially by salary reduction and 1) the amount contributed by your employer is less than half the amount you set aside through salary reduction, 2) you receive the 2004 EITC for families with a qualifying child, and 3) your 2004 adjusted gross income (after subtracting any amount attributable to your participation in a DCAP) is less than \$15,000 (if you are single) or \$16,000 (together with your spouse's adjusted gross income, if you are married), you may actually lose 2004 federal EITC benefits by participating in a DCAP instead of claiming the DCTC.

Because of the interaction between DCAP participation and the EITC, many but not all families who receive the EITC benefit more from participating in a DCAP than from claiming the DCTC.



#### What is the combined value of these tax benefits?

You can claim the DCTC, CTC and EITC if you meet the eligibility requirements for each provision. As described above, participating in a DCAP may affect the amount of your DCTC, EITC, or CTC.

#### Example

If you are married, you have two qualifying children, and you (together with your spouse) have \$55,000 in adjusted gross income (before taking into account any salary reduction that may occur because of your participation

in a DCAP) and \$5,000 in child care expenses in 2004, you can receive \$1,133 by participating in a DCAP and \$2,000 by claiming the CTC, for total 2004 federal tax savings of \$3,133.

## How to Claim these Tax Benefits and Get More Information About Them and Similar State Tax Benefits

*What do I need to do to claim the DCTC or to receive benefits through a DCAP?*

To claim the DCTC, you must file a tax return. If you were married at the end of 2004, you generally must file a joint return, although special rules apply if you lived apart from your spouse. You must file either Form 1040 or 1040A (not 1040EZ) and a separate form or schedule with your tax return. With Form 1040, file Form 2441. With Form 1040A, file Schedule 2. Form 2441 and Schedule 2 do not come with either Form 1040 or 1040A; they are available at <http://www.irs.gov/formspubs/index.html>. Note that IRS forms and instructions refer to the DCTC as the "Credit for Child and Dependent Care Expenses."

To benefit from a DCAP, your employer must offer a DCAP and you must participate in it. You must also report the amount of your DCAP benefits on your tax return. You must file either Form 1040 or 1040A (not 1040EZ) and Form 2441 (with Form 1040) or Schedule 2 (with Form 1040A). The amount of any DCAP benefits you received during 2004 should be provided by your employer in Box 10 of your W-2 form.



To claim the DCTC or benefit from a DCAP, you must provide a Social Security Number (SSN) or an Individual Taxpayer Identification Number (ITIN) for yourself, your spouse if you are married, and any qualifying child or dependent. To apply for an SSN, you must complete Form SS-5 from the Social Security Administration, which is available at <http://www.ssa.gov/online/ss-5.html>. It can take some time to receive an SSN, so apply well in advance of the date you want to file your tax return. You must complete Form W-7, which is available from the IRS at <http://www.irs.gov/pub/irs-fill/fw7.pdf>, and you must file your tax return along with Form W-7 to apply for an ITIN. If you file your tax return along with an ITIN application, you should send both to the address given in the Form W-7 instructions, not to the address listed in Form 1040, 1040A or 1040EZ instructions.

To claim the DCTC or benefit from a DCAP, you must also have basic information about your provider, including the provider's name, address, and, if the provider is not a tax-exempt organization, an identification number (the provider's SSN or Employer Identification Number). If you have tried to get your provider's identification number but have not been successful, you can explain on your return that you asked for the information but the provider did not comply with your request.

#### *What do I need to do to claim the CTC?*

Even if you don't owe any federal income taxes, you must file a tax return to claim the CTC. You must file either Form 1040 or 1040A (not 1040EZ). You must provide an SSN or an ITIN for yourself, your spouse if you are married, and any qualifying child. If your 2004 adjusted gross income is above \$75,000 (if you are single) or above \$110,000 (together with your spouse's adjusted gross income, if you are married), you must also use a worksheet in Publication 972. To claim the refundable component of the CTC, you must also file Form 8812. Publication 972 and Form 8812 do not come with either Form 1040 or 1040A; they are available at <http://www.irs.gov/formspubs/index.html>.

#### *What do I need to do to claim the EITC?*

Even if you don't owe any federal income taxes, you must file a tax return to claim the EITC. If you were married at the end of 2004, you must file a joint return. If you have a qualifying child, you must file either Form 1040 or 1040A (not 1040EZ) and a separate form, Schedule EIC. Schedule EIC does not come with either Form 1040 or 1040A; it is available at <http://www.irs.gov/formspubs/index.html>. If you have no qualifying children, you may file either Form 1040, 1040A or 1040EZ. You must provide an SSN for yourself, your spouse if you are married, and any qualifying child. (Note that you may not use an ITIN to claim the EITC.) If you can provide the basic information to show your eligibility, the IRS will calculate your EITC for you if you write "EIC" next to line 65a on Form 1040, or line 41a on Form 1040A, or line 8a on Form 1040EZ.

To receive a portion of your EITC in advance—that is, in your paycheck each pay period—complete Form W-5 and give it to your employer. You can give Form W-5 to your employer at any time during the year, but you should do so as early in the year as possible to begin receiving advance EITC benefits promptly. If you receive advance EITC benefits, you must file a tax return at the end of the year in order to receive the rest of your EITC benefits. Remember that you must have a qualifying child to receive advance EITC benefits. Remember also, if you elect to receive advance EITC benefits, the amount of any tax refund you could be eligible for at the end of the year will be lower than if you had waited to take all of the EITC when you file your return.

A small number of taxpayers who claimed the EITC for a qualifying child in 2003 will be asked by the IRS to verify that their qualifying children lived with them for more than half of 2004 in order to claim the EITC for 2004. Only taxpayers who receive a specific notice from the IRS telling them that they need to submit Form 8836 are required to provide this additional information in order to claim the EITC.

*How can I get more information about these tax benefits and similar state tax benefits?*

For more information on the federal tax benefits, you can call the Internal Revenue Service at 1-800-TAX-1040 toll free or contact your local IRS Regional Manager for a current list of Volunteer Income Tax Assistance (VITA) clinics where you can get free help in filing your tax return. You can also visit the IRS web site, which provides tax forms, instructions, and other publications to assist you in filing your return, [www.irs.gov](http://www.irs.gov).

For more information about similar state credits, check with your state department of revenue or the instructions for your state income tax return, or visit [www.taxadmin.org/fta/link/forms.html](http://www.taxadmin.org/fta/link/forms.html), which provides links to state departments of revenue and tax forms for all the states. The National Women's Law Center's publication, *Making Care Less Taxing*, provides information on state child and dependent care credits and deductions, available at [www.nwlc.org/mclt](http://www.nwlc.org/mclt); the Center on Budget and Policy Priorities' paper, *A Hand Up*, provides information on state earned income tax credits, available at [www.cbpp.org/5-14-04sfp.htm](http://www.cbpp.org/5-14-04sfp.htm).

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