Dependent Care Benefit and Form W-2 Block 10

Form W-2 Block 10 is for Dependent Care Benefits and reports a benefit provided by the Employer to the Employee under a Dependent Care Assistance Program (DCAP) under IRS Section129. The Block 10 entry shows the total amount of dependent care benefits that the Employer provided to the Employee or incurred on behalf of the Employee. The benefit is generally tax-free to the Employee if under the established limits. The limit had been $5000 and the American Rescue Plan increased this to $10,500 for 2021. If the benefit exceeds the limit, then some of the benefit can be taxable to the Employee.

The benefit can be provided in three general ways:

1. Benefits provided in kind by the employer at the established fair market value, or
2. Benefits paid directly to a care provider by the employer or reimbursed to the employee to subsidize the benefit, or
3. Benefits from the pre-tax contributions made by the employee under a dependent care flexible spending account (FSA).

Typically, these benefits are provided using method 3 above. The dependent care FSA (DCAP), is an employer-sponsored benefit plan that allows Employees to pay for certain dependent care expenses on a tax-free basis, up to a specified limit. In most cases, the dependent care FSA is funded by Employees with pre-tax dollars through payroll deductions (IRS Section 125 salary reduction agreements). It is possible that an Employer could also contribute to the Employee's dependent care FSA. When Employees incur eligible dependent care expenses, such as expenses for babysitting or child care, they can seek reimbursement from their dependent care FSA account. The dependent care FSA is similar to a health FSA, but each has its own rules.

Since the DCAP or dependent care FSA, is provided as tax-free money to the Employee, it cannot in-turn be used for the Dependent Care Credit. The net out-of-pocket cost of the dependent care for the Employee is typically the difference between the amount paid to the child care provider and the amount of the tax-free benefit as shown in Block 10. This net out-of-pocket cost is what the Dependent Care Credit is based on.

The Dependent Care Credit on a tax return is calculated using Form 2441, Child and Dependent Care Expenses. TaxSlayer labels this entry as the "Child Care Credit". The initial TaxSlayer entry for the "Amount Paid to Provider for Child Care" (also means Dependent Care) says: "Enter the total amount paid to provider, including amounts from W-2, Box 10". This statement can be confusing and it can be unclear how to calculate this amount. Generally, you should use the amount on the statement from the Child Care Provider. If there are any questions, it is recommended that you interview the taxpayer and understand how the W-2 Block 10 entry was paid. Also understand if the statement from the Child Care Provider included payments paid directly by the Employer – this should be detailed on the statement if applicable.

Once this is understood, it should be clear on how to make the TaxSlayer entry. Simply, this entry is supposed to reflect the total paid to the provider. The Form 2441 treats any entry from the W-2 Block 10 as an excluded benefit. The Form 2441 also calculates any taxable benefit if the limit is exceeded.

The NTTC Workbook contains scenarios for this situation and usually provides little information on who paid what to the care provider. Typically, a statement from the care provider is given with the total paid along with a W-2 with a Block 10 entry. Experience has shown that the correct NTTC answer is obtained using the amount paid from the statement as the entry amount for the total amount paid to provider. Do not add the W-2 Block 10 amount. The Form 2441 will exclude the W-2 Block 10 entry and correctly calculate the credit.

The Dependent Care credit on the federal return is limited to $3000 per child for one child and $6000 for more than one child. Idaho allows the Child and Dependent care expense to be taken as a deduction. Up to a $12,000 deduction is allowed on the Idaho without regard to the number of children claimed. TaxSlayer carries up to $3000 (for a single child dependent) and $6,000 (for more than one child) but has no provision for claiming dependent care expenses above these dollar limits to the Idaho return. If actual dependent care expenses exceed the $3000 (or $6000 for more than one child) the difference must be added to the Idaho return using form the TaxSlayer State return menu.

Also. note that this federal credit and state deduction can be claimed for disabled dependents, e.g., severe dementia, Alzheimer's, who are over age 13 if the care is necessary to allow the taxpayer (s) to work.