How to Reduce Employee's Child Care Costs

DECAL
Thriving Child Care
Business Academy

Learn how to offer child care as a benefit to employees of your child care business

In today's competitive business landscape, offering meaningful benefits can significantly enhance employee satisfaction and retention. For child care business owners, providing free child care to their own employees is not just a perk, but a powerful statement of support and understanding of their needs.

Why cover child care costs?

Employer-provided child care support can have multiple benefits. First, it provides crucial financial relief for families, reducing the weight of childcare expenses and allowing parents to allocate resources to other essential needs. Second, there are multiple impacts on recruitment and retention by providing employees with:

- Improved work-life balance;
- Competitive benefits; and
- Reduced absenteeism and stress.

This guide explores three viable approaches to achieve this: through Dependent Care Flexible Spending Accounts (FSAs), direct payment as a taxable benefit, and in-kind provision of child care services.

How can I reduce the cost of child care?

Option 1: *Using Dependent Care Flexible Spending Accounts (FSAs)*

Dependent Care FSAs are a versatile option for employees to manage child care costs. By allocating pre-tax earnings into these accounts, employees can pay for eligible dependent care expenses, which can range from full-day child care to after-school programs. While primarily funded by employees, employers can also contribute, increasing the benefit's appeal.

Typically, the Dependent Care FSA funds can cover the care of expenses for children under the age of 13. However, it can also cover expenses for a spouse or a dependent of any age (including children, but also parents) who is physically or mentally incapable of self-care.

The major advantage of Dependent Care FSAs lies in their tax benefits. Employees' contributions decrease their taxable income. The numbers can add up. In 2024, the annual contribution limit is $5,000 for individuals or married couples filing jointly, and $2,500 for a married person filing separately.

For employers, the attractiveness of Dependent Care FSAs is in their dual role as a tax-efficient benefit, because the contributions and costs are deductible, and a tool for increasing employee satisfaction by addressing a major family concern — affordable care.

However, there are two issues with Dependent Care FSAs. First, typically they take time and money to launch and maintain. Second there is a "use-it-or-lose-it" policy which means that any unused funds at the end of the calendar year are forfeited.

Option 2: *Direct Payment of Child Care Expenses*

Another approach is for employers to pay directly for their employees' child care expenses. In this method, typically the employer provides a set amount each pay-period for child care (such as $200 a month).

This direct payment method results in a tax deduction for employers. Employers also have greater discretion over how the money is spent. For example, they could limit contributions to children under five.

Employees often like this option because of its simplicity and also because it doesn't depend on making their own contributions to a formal vehicle like a Dependent Care FSA. However, the challenge with direct payment is that these kinds of benefits are considered taxable. So, the employee does not receive a tax benefit and the payments are treated the same as any other wages.

Option 3: *Providing In-Kind Child Care Services*

The third option involves employers providing child care services directly to their employees for no or reduced cost. This can be executed through on-site facilities or by contracting with child care providers.

Employees typically appreciate this benefit because it is simple to understand and easy for them to access. From a tax perspective, in-kind child care services are generally not considered taxable income for employees, so they have no increased tax burden with this option.

For employers, the costs can be high if they provide on-site care. Even a child care business can have the costs of having to engage additional staff to accommodate employees' children. If choosing to offer care for your employees at your child care business, you'll want to consider the impacts the additional costs will have on your operations.

If you are offering on-site care, you may be eligible for tax credits to offset some of these costs if 30% or more of the children cared for are employees'. In this case, the employer may be eligible for tax credits related to the expenses of operating a child care facility. The credit, known as the Employer-Provided Child Care Credit (Form 8882), offers a percentage of the expenses incurred in operating a qualified child care facility.

It is important to note that while the costs of providing free or reduced cost care for employees are deductible, the actual discount itself is not. For example, let's say Claudia owns a small center. She provides free care to her ten employees. If she normally charges $1,444.50 per month, the benefit means she's potentially losing $14,445 per month in revenue. However, she cannot deduct this loss. She can deduct the cost of her operations such as paying teachers, food, transportation, etc.

	Pros	Cons
Dependent Care FSA *Pre-tax financial account used to pay for eligible dependent care*	• Tax benefits for employees and employers	• Can be complex and funds can be forfeited if not used
Direct Payment *Straightforward payment from employers*	• Simplifies access to child care	• Additional taxable income
Providing In-Kind Services *Employers provided child care services*	• Tax benefits for employees and employers	• Lost revenue can be high

And don't worry about "de minimus" benefits

In the context of employer-provided child care, the concept of "de minimis" benefits refers to any benefit that is so small as to make accounting for it unreasonable or administratively impractical. The IRS generally excludes de minimis benefits from an employee's taxable income. However, the application of this concept can be quite specific and depends on the circumstances. Here's how it might apply in scenarios related to employer-provided child care:

- Occasional babysitting or emergency child care
- Small, infrequent benefits (i.e. snacks)
- Limited child care subsidies

Conclusion

Each of these methods offers unique advantages and challenges. Dependent Care FSAs provide tax efficiency and flexibility but can be complicated and costly; direct payments offer simplicity and immediate support but are taxable; and in-kind services can incur costs for the employer, but are deductible and, for employees, tax free. Child care business owners should consider their specific circumstances, employee needs, and organizational capabilities when choosing the best approach.

Additional Resources

If you have questions or need help, assistance is available.
GaPDS Website
DECAL Thriving Child Care Business Academy Website
To Find Other Study Guides: Click on Resources on the Academy home page
To Find Training: Click on Trainings on the Academy home page
To Register for Training: Click on Schedules & Registration on the Academy home page
To Sign Up for Study Groups: Fill out the Intake Assessment
For questions about coaching or study groups: Email GAcoaching@civstrat.com
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Family Child Care Learning Home Rules and Regulations
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