

Checkpoint Contents
Federal Library
Federal Editorial Materials
United States Tax Reporter
Income (USTR)
Determination of Tax Liability §§1-59B
Business Related Credits §§38-45Q
§45F Employer-provided child care credit
Explanations for Code Sec. 45F
EXP ¶45F4 Employer-provided child care credit.

Code Arranged Explanations

EXP ¶45F4 Employer-provided child care credit.

There is available an “employer-provided child care credit.” [Code Sec. 45F\(a\)](#).

The credit, which is part of the [Code Sec. 38](#) general business credit, see [¶384](#) et seq., is equal to the sum of the following expenditures of the taxpayer for the tax year:

- (1) 25 percent of the “qualified child care expenditures” (defined below) and
- (2) 10 percent of the “qualified child care resource and referral expenditures” (defined below). [Code Sec. 45F\(a\)](#).

 **OBSERVATION:** The “taxpayer” referred to above is the employer that provides child care assistance. It is the employer that receives the credit if all of the rules discussed below are satisfied.

The amount of the credit cannot exceed \$150,000 for any tax year. [Code Sec. 45F\(b\)](#).

Example 1. X Corporation (“X”), which uses the cash method, pays, in Year 1, \$800,000 of “qualified child care expenditures” and \$300,000 of “qualified child care resource and referral expenditures.” Twenty-five percent of \$800,000 plus 10% of \$300,000 is \$230,000 (i.e., \$200,000 plus \$30,000). Nevertheless, X’s employer-provided child care credit for Year 1 can’t exceed \$150,000.

For the effect after Dec. 31, 2010 on the rules discussed above of sunset provisions contained in Sec. 901, PL 107-16, 6/7/2001, see [¶79,006.86](#).

Qualified child care expenditures.

Except as limited by the fair market value rule discussed below, a “qualified child care expenditure” is any amount paid or incurred:

- (1) to acquire, construct, rehabilitate, or expand property:
 - which is to be used as part of a “qualified child care facility” (defined below) of the taxpayer,
 - with respect to which a deduction for depreciation (or amortization in lieu of depreciation) is allowable, and

- which isn't part of the principal residence (within the meaning of [Code Sec. 121](#), see [§1214](#)) of the taxpayer or any employee of the taxpayer;

(2) for the operating costs of a “qualified child care facility” of the taxpayer, including costs related to the training of employees, to scholarship programs, and to the providing of increased compensation to employees with higher levels of child care training; *or*

(3) under a contract with a “qualified child care facility” to provide child care services to employees of the taxpayer. [Code Sec. 45F\(c\)\(1\)\(A\)](#).

Qualified child care expenditures do not include expenses in excess of the fair market value of the care. [Code Sec. 45F\(c\)\(1\)\(B\)](#).

 **TAX TIP:** In the absence of IRS guidance as to how to comply with the fair market value limit, taxpayers should consider taking steps to lessen the risk of non-compliance (and, thus, the risk of losing part of the credit). For example, in conducting their search for child care providers, taxpayers should consider choosing from a large field of candidates and maintaining thorough records of the search process (e.g., records pertaining to information gathering, interviewing, negotiating, etc.).

Qualified child care facility.

A “qualified child care facility” is a facility:

- (1) the principal use of which is to provide child care assistance, and
- (2) which meets the requirements of all applicable laws and regulations of the State or local government in which it is located, including the licensing of the facility as a child care facility. [Code Sec. 45F\(c\)\(2\)\(A\)](#).

The principal use requirement doesn't apply to a facility which is the principal residence (within the meaning of [Code Sec. 121](#)) of the operator of the facility. [Code Sec. 45F\(c\)\(2\)\(A\)](#).

 **OBSERVATION:** Thus, the fact that a child care facility is located in a residence doesn't prevent an otherwise-qualifying facility from being a “qualified child care facility.” However, as discussed above, if the taxpayer or its employee uses the qualified child care facility as a principal residence, certain costs don't qualify as “qualified child care expenditures.”

A facility won't be treated as a qualified child care facility with respect to a taxpayer-employer unless:

- enrollment in the facility is open to employees of the taxpayer during the tax year,
- if the facility is the principal trade or business of the taxpayer, at least 30 percent of the enrollees of the facility are dependents of employees of the taxpayer, and
- the use of the facility (or the eligibility to use the facility) doesn't discriminate in favor of employees of the taxpayer who are highly compensated employees (within the meaning of [Code Sec. 414\(q\)](#), see [§4144.21](#)). [Code Sec. 45F\(c\)\(2\)\(B\)](#).

Qualified child care resource and referral expenditures.

A “qualified child care resource and referral expenditure” is any amount paid or incurred under a contract to provide child care resource and referral services to an employee of the taxpayer. [Code Sec. 45F\(c\)\(3\)\(A\)](#). However, the services aren't treated as qualified unless the provision of the services (or the eligibility to use the services) doesn't discriminate in favor of employees of the taxpayer who are highly compensated employees (within the meaning of [Code Sec. 414\(q\)](#)). [Code Sec. 45F\(c\)\(3\)\(B\)](#).

Basis reductions.

Where the credit is determined with respect to any property by reason of expenditures described in [Code Sec. 45F\(c\)\(1\)\(A\)](#) (see “Qualified child care expenditures” above), the basis of that property must be reduced by the amount of that credit. [Code Sec. 45F\(f\)\(1\)\(A\)](#). Thus, if employer-provided child care credits are claimed for expenses of acquiring, constructing, rehabilitating, or expanding a facility, the taxpayer's basis in the facility is reduced by the amount of the credits. Conf Rept No. 107-84 (PL 107-16) p. 139, at [¶45F1.1](#).

 **OBSERVATION:** Presumably, as indicated by the Conference Report, the basis reduction rule is intended to apply only to costs that would otherwise be included in the basis of property. Other costs described in [Code Sec. 45F\(c\)\(1\)\(A\)](#), for example costs of operating a qualified child care facility, are, presumably, subject only to the rule (see “Denial of other tax benefits” below) that reduces deductions and other credits by the amount of the [Code Sec. 45F](#) credit claimed for the costs.

Example 2. T, an employer, using the cash method, pays, in Year 1, \$420,000 of costs of constructing and acquiring property that is used as part of a qualified child care facility. All of the costs qualify as “qualified child care expenditures” under [Code Sec. 45F\(c\)\(1\)\(A\)](#), and T claims an employer-provided child care credit of \$105,000 ($\$420,000 \times 25\%$) with respect to these construction and acquisition costs. T also pays, in Year 1, \$100,000 of costs of operating the facility, all of which qualify as “qualified child care expenditures” under [Code Sec. 45F\(c\)\(1\)\(A\)](#), and T claims an employer-provided child care credit of \$25,000 ($\$100,000 \times 25\%$) with respect to these operating costs.

T must reduce its basis in the property by \$105,000. For additional tax consequences, see Example 3 below.

For a rule under which, where the credit is recaptured, all or part of the above basis reduction is added back to basis, see [¶45F4.01](#).

Denial of other tax benefits.

No deduction or credit is allowed under any other income tax provision with respect to the amount of the credit determined under [Code Sec. 45F](#). [Code Sec. 45F\(f\)\(2\)](#). Thus, any amounts for which the taxpayer may otherwise claim a tax deduction are reduced by the amount of the credit. Conf Rept No. 107-84 (PL 107-16) p. 139, at [¶45F1.1](#).

Example 3. The facts are the same as in Example 2. T can claim only \$75,000 [$\$100,000$ minus $\$25,000$] of deductions with respect to the \$100,000 of operating costs.

Example 4. The facts are the same as in Example 2, except that T also pays, in Year 1, \$200,000 of “qualified child care resource and referral expenditures” (see above). T claims an [Code Sec. 45F](#) credit in an amount of \$20,000 ($\$200,000 \times 10\%$) for these expenditures.

T can claim only \$180,000 [i.e., \$200,000 minus \$20,000] of deductions with respect to the \$200,000 of expenditures.

Recapture.

For rules that require recapture of all or part of the [Code Sec. 45F](#) credit where a qualified child care facility is disposed of by the taxpayer or ceases to be operated as a qualified child care facility, see [§45F4.01](#).

Aggregation of multiple employers.

For purposes of [Code Sec. 45F](#), all persons treated as a single employer under (1) [Code Sec. 52\(a\)](#) or [Code Sec. 52\(b\)](#) (which treat employees of certain employers as employed by the same employer for purposes of the work opportunity credit, see “Commonly controlled businesses” at [§1514](#)) or (2) [Code Sec. 414\(n\)](#) or [Code Sec. 414\(o\)](#) (relating to employee leasing, see [§14144.19](#)), are treated as one taxpayer. [Code Sec. 45F\(e\)\(1\)](#).

 **OBSERVATION:** Thus, employers that are treated as a single taxpayer, are allowed *in the aggregate* no more than \$150,000 of [Code Sec. 45F](#) credits per tax year.

Allocations between an estate or trust and its beneficiaries.

Under regs to be issued by the IRS, rules similar to the rules in [Code Sec. 52\(d\)](#) will apply to the [Code Sec. 45F](#) credit. [Code Sec. 45F\(e\)\(2\)](#).

 **OBSERVATION:** Presumably, these regs will provide that the [Code Sec. 45F](#) credit is apportioned between an estate or trust and its beneficiaries in accordance with the income of the estate or trust allocable to each, see [Code Sec. 52\(d\)](#).

Allocations among partners.

In the case of partnerships, the credit will be allocated among partners under regs to be issued by the IRS. [Code Sec. 45F\(e\)\(3\)](#).

Election and allocation of the credit.

 **OBSERVATION:** [Code Sec. 45F](#) doesn't say whether the employer-provided child care credit is by election of the employer. Also, if the credit is elective, IRS guidance as to how to elect the credit would seem necessary. This guidance might provide that a taxpayer elects out of the credit by not claiming it on its tax return (which is the method that a taxpayer uses to elect out of the work opportunity tax credit, see [§1514](#)).

 **OBSERVATION:** If the credit is elective, in most cases it will be advantageous for employers to claim the credit (rather than elect out of the credit). But, some employers

might reduce their overall tax liability by electing out of the credit because the credit (1) can't be used against the alternative minimum tax and (2) sometimes can't be used against the regular income tax, see [§1514](#).

 **OBSERVATION:** [Code Sec. 45F](#) does not address whether employers are permitted to choose the qualifying expenditures for which they claim the credit, where, as in Example 1 above, the sum of 25 percent of the employer's "qualified child care expenditures" for the tax year and 10 percent of the employer's "qualified child care resource and referral expenditures" for the tax year is greater than the \$150,000 annual limit on the credit.

 **TAX TIP:** If taxpayers can choose the qualifying expenditures for which they claim the credit, generally, they should choose to claim the credit for expenditures which must be capitalized instead of for expenditures which can be immediately deducted. This is so because the reduction in other tax benefits required under the rules discussed under "Basis reductions" above, and "Denial of other tax benefits" above, if evaluated on a present value basis, will be generally less for the expenditures which must be capitalized. Similarly, taxpayers should choose to claim the credit for capitalized expenditures that are for property with longer MACRS recovery periods (e.g. a building), rather than for capitalized expenditures that are for property with shorter MACRS recovery periods (e.g. furniture). This is so because the reduction in other tax benefits required under the rules discussed under "Basis reductions" above, if evaluated on a present value basis, will be generally less for the expenditures for property with a longer recovery period.

There are, however, factors which can, in a particular case, cause the above general guidelines not to apply—for example, a strong possibility that the taxpayer will shortly dispose of a "qualified child care facility" (leading to recapture of credits, see [§145F4.01](#)).

Prior law.

For tax years beginning before Jan. 1, 2002, the employer-provided child care credit wasn't available. [Sec. 205\(c\), PL 107-16, 6/7/2001](#).