

Tax Breaks

Good News: Tax Breaks Can Offset — Sometimes Exceed — Your Employer Tax Costs

A Complimentary Resource from
Breedlove & Associates

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While most families are excited to find that perfect person to help care for their loved ones, the euphoria quickly disappears when they think about payroll taxes. Most people assume that payroll taxes will significantly increase the cost of being a household employer.

Well, we have good news: they're wrong! The truth is, for most employers, tax breaks offset virtually all of the employer payroll taxes. And for many, the tax savings actually exceed the cost of employer taxes – meaning employers actually come out ahead by paying their household employees legally! See table below for estimates by salary level.

| Effect of Tax Breaks by Salary Level | | | | | |
|--------------------------------------|--------------------------------------|------------------------------|---------------|------------------------------------|---------------|
| Employee's Annual Gross Salary | Employer's Annual Tax Obligation (b) | Savings from Tax Breaks! (a) | | After Tax Savings/(Cost) (a - b =) | |
| | | 1 Dependent | 2+ Dependents | 1 Dependent | 2+ Dependents |
| \$12,000 | \$1,217 | \$2,300 | \$2,500 | \$1,083 | \$1,283 |
| \$18,000 | \$1,676 | \$2,300 | \$2,500 | \$624 | \$824 |
| \$24,000 | \$2,135 | \$2,300 | \$2,500 | \$165 | \$365 |
| \$30,000 | \$2,594 | \$2,300 | \$2,500 | (\$294) | (\$94) |
| \$36,000 | \$3,053 | \$2,300 | \$2,500 | (\$753) | (\$553) |

Calculations based on 2007 tax tables and average state taxes. Actual tax savings will vary slightly by state. Assumes utilization of Dependent Care Account and a marginal tax rate of 45%.

Available Tax Breaks

A tax break is available to you if you hire a nanny, tutor, personal attendant, or housekeeper whose services are at least partly for the well-being and protection of your dependent. To qualify for a tax break, your household employment must meet the work-related expense test. This means that if an individual is employed to care for a child under the age of 13, both you and your spouse must work; or if household services are provided for one spouse, the other spouse must work; or if household services are provided for your parent you claim as a dependent, you must work. If you qualify, you have two tax breaks available:

- **Dependent Care Account.** Also called a Flexible Spending Account (FSA). If you work for a participating company, you can contribute up to \$5,000 of your pre-tax earnings per family per year to a FSA. Because you're setting aside pre-tax dollars, you'll save federal income taxes, state income taxes, Social Security and Medicare taxes. Depending on your tax bracket, this tax break can put as much as \$2,300 per year in your pocket. For details on your eligibility, check with your HR or Accounting Department.
- **Child or Dependent Care Tax Credit.** You're entitled to a 20% tax credit on expenses of up to \$3,000 for one dependent (\$600 savings) or up to \$6,000 for 2 or more dependents (\$1,200 savings). You can claim this tax credit by completing IRS Form 2441 as part of your personal income tax return at year end.

Maximizing Your Tax Breaks

- **If you have one dependent,** your best option is the FSA. Set aside the full \$5,000 (if your expenses were \$5,000 or more). You'll save between \$2,000 and \$2,300 per year, depending on your tax bracket and which state you live in. If you don't have access to a FSA (or cannot enroll until a future tax year), utilize the Tax Credit. You are not entitled to both breaks.
- **If you have two or more dependents,** set aside the full \$5,000 into your FSA (if your expenses were at least \$5,000). This will save you between \$2,000 and \$2,300 per year, depending on your tax bracket and which state you live in. If your dependent care expenses were greater than your FSA contribution, you have "excess expenses." These excess expenses can be applied to the Tax Credit on Form 2441 and save you up to an additional \$200 per year. For a typical family, combining the FSA and Tax Credit savings will result in a total annual tax break between \$2,200 and \$2,500.

At Breedlove & Associates, we provide comprehensive payroll & tax service, making it easy to pay legally and maximize your tax breaks. And, by the way, a little more good news: our fees – which are about \$1.50 a day – are tax deductible.

If you have any questions about your specific tax break options, please call 888-BREEDLOVE (273-3356). We're here to help.

