Increased Uptake of Business Tax Cuts Could Help Address Child Care Shortages

Parents in the United States face a child care system plagued by workforce shortages, long waiting lists, and expensive care. Parents can wait as long as two years for a child care slot that costs $13,184 a year on average per child across age and type of care, and often costs much more. Businesses, the economy, and the strength of America's workforce suffer due to these challenges. The Bipartisan Policy Center estimates that the lack of affordable and reliable child care will cost the U.S. economy as much as $329 billion over the next ten years. This cost is paid for by families and businesses alike, including through:

- A drop in family income when parents are forced to leave the workforce or cut back on their hours due to the lack of affordable or available child care;
- Higher costs for businesses due to staff turnover that requires businesses to spend time and money on hiring and training replacement workers;
- Decreased productivity for businesses when parents are late or must miss work due to lack of child care.

Over the years, Congress has worked in a bipartisan way to incentivize businesses to provide or contribute to the child care needs of their employees. Yet only 13 percent of private sector workers are offered child care benefits through their employer, and current tax incentives are underutilized due to a lack of awareness about the programs and their complex rules. This Joint Economic Committee – Minority report lays out ways that businesses and their employees can save money through increased use of already-existing child care tax cuts. It makes the case for measures including the proposed bipartisan *Child Care Tax Benefit Outreach and Assistance Act*, which would help more businesses and families save money on their taxes and get more children the high-quality, reliable care that they need.

Underutilization of Current Child Care Tax Cuts for Businesses and Their Employees

Reports from both the Government Accountability Office and Congressional Research Service find that child care tax cuts for businesses and their employees are underused and difficult to navigate. These tax cuts include:

- **45F:** Businesses can use 45F, the employer-provided child care tax credit, to help offset some of the costs of providing child care. Under this program, businesses that invest in child care for their employees can subtract 40 percent (or 50 percent for small businesses) of certain expenses from the amount that they owe in taxes, up to a maximum of $500,000 in tax savings (or up to $600,000 for small businesses). These allowable expenses include building and operating a child care facility on-site or partnering with existing child care providers to increase access to care and lower costs for their employees. Despite this opportunity for tax savings, tax filing data from 2016 – the most recent data available – show that less than 1 percent of corporate returns used the 45F program.

- **Dependent Care Assistance Program (DCAP):** Businesses can set up DCAP accounts for their employees, which enables the employees to lower the amount they owe in taxes. DCAPs allow families to save money by setting aside up to $7,500 of pre-tax income for child care expenses. Families do not pay taxes on these funds if they are spent on child care or other allowable expenses. Despite this benefit, less than half of private sector workers have access to DCAP accounts.
- **Child and Dependent Care Tax Credit (CDCTC):** Workers can also get a tax cut for child care expenses through the CDCTC. This program lets families subtract some of what they spend on child care each year from the amount they owe in federal income tax. For example, a family who pays the national average cost for child care and who earns $70,000 and has one child could get a $1,050 tax cut. Despite the meaningful opportunities for savings, only about 12 percent of taxpayers with children use the Child and Dependent Care Tax Credit. The rest of these taxpayers either do not have qualifying expenses, owe no federal taxes, make too much money to qualify, or have trouble navigating the credit despite being eligible.

One solution to increase the utilization of these programs and reduce expenses for hardworking families is the newly introduced bipartisan *Child Care Tax Benefit Outreach and Assistance Act*, led by Senator Maggie Hassan, Ranking Member of the Joint Economic Committee, and Senator Dan Sullivan. This bill would create a dedicated liaison at the Internal Revenue Service (IRS) to provide targeted outreach, education, and assistance to businesses about child care tax cuts that will help them retain workers and lower costs. The legislation would also strengthen relationships between the business community and child care community to help break down barriers to improving access to child care. While this IRS liaison alone would not solve the child care affordability crisis, it represents a meaningful, commonsense step toward helping lower costs for families and helping businesses recruit and retain a strong workforce. With the help of a Business Child Care Liaison at the IRS, more businesses and families could reap the full benefits of child care tax cuts.

Calculating the Economic Benefit of Child Care Tax Cuts for Businesses

Given the challenges that businesses face when their employees struggle to find child care, studies have found that employer-provided child care programs pay for themselves through increased employee retention, more hours worked, and increased productivity. Every $1 invested by a business in employer-provided child care returns an average of $2.90 in benefits to the employer.

To illustrate the potential benefits of a new IRS liaison focused on increasing businesses' use of the child care tax cuts, the Joint Economic Committee – Minority spoke with experts and business leaders to explore two example scenarios.

Example Scenario 1: New Child Care Facility

Business A wants to increase access to child care for parents among its 700 employees, but notes that there are few affordable providers in the surrounding community. After consulting resources provided by the Business Child Care Liaison at the IRS, the business decides to leverage the 45F program to build an on-site child care facility and then helps employees leverage the Dependent Care Assistance Program and Child and Dependent Care Tax Credit to further save money.

This scenario involves large upfront costs because the business has to build or retrofit existing space to accommodate a new child care facility. To better account for how the return-on-investment and family cost savings accumulate over time, this analysis looks at a five-year period for both the costs and benefits.

Business Costs

- The U.S. Government Accountability Office estimates that building a new child care facility costs between $1 and $3 million. As a result, this scenario assumes that Business A spends $2 million up front during year one to build and operate the facility.
- Based on conversations that the Joint Economic Committee – Minority had with large businesses about the operational costs of running their own child care facilities, this scenario then assumes that the company spends $200,000 in each later year to operate the facility. During the four-year period that the child care center is open, Business A spends $800,000 on operational costs.
- In total, the business spends $2.8 million over the first five years to help provide on-site child care to its employees.

Business Savings

Through the 45F program, this example large business can reduce the amount it owes in corporate income tax by an amount equal to 40 percent of its qualified spending on child care each year, capped at $500,000 per year for a business of this size.

- **As a result, Business A can lower the amount of taxes it owes by $500,000 in the first year and $80,000 in subsequent years.** These savings would amount to $820,000 over five years, or nearly a third of the cost of opening and operating a child care facility for its employees.
- Assuming that Business A sees a $2.90 average return-on-investment from employer-sponsored child care, the company's $2.8 million investment in child care for their employees over five years would yield them **an additional $8.1 million in benefits** from reduced employee turnover and increased productivity.

Family Child Care Savings

Based on conversations that the Joint Economic Committee – Minority had with businesses that provide child care to their employees, this analysis assumes that the business sets the price of child care at their on-site facility 5 percent below the national average annual cost of child care of $13,184, so $12,525 per year for employees at Business A. For this example scenario, the Committee assumes that Business A employees are in a household with one child and no other working parent.

Before using tax credits, employees are saving $659 per year on child care after the facility is operational because the business is offering child care at a cost below the national average. In addition, employees can take advantage of Business A's Dependent Care Assistance Program (DCAP) as well as the Child and Dependent Care Tax Credit during all five years. Recent U.S. Department of Treasury data show that most middle-class workers received roughly $400 in tax benefits from these types of programs, which would mean that they put aside approximately $1,350 in pre-tax contributions to Dependent Care and Assistance Program accounts.

- Because this $1,350 in contributions to a Dependent Care and Assistance Program account does not get taxed, each participating employee at Business A **now will pay $400 less in taxes each year than they would have if they did not use a DCAP account.**
- Families can then get a tax cut based on a portion of their remaining child care expenses through the Child and Dependent Care Tax Credit during each of the five years. With one dependent and remaining child care expenses of at least $3,000, each family can **lower the amount they pay in taxes by an additional $1,050 each year.**

Thus, in total, Business A saves $820,000 and an employee at the business saves $9,887 during the five years. The employee's savings are the equivalent of 15 percent of the national annual average price of child care over these five years. These savings also do not account for other money that employees may have otherwise lost if they had been forced to miss work or leave the labor force altogether due to a lack of child care.

Example Scenario 2: Helping Cover Child Care Costs

Business B wants to increase access to child care for parents among its 2,500 employees. It notes that while there are many providers in their area, the cost of child care is too expensive for many of its employees. After leveraging information provided by the IRS' Business Child Care Liaison, the business decides to use the 45F program to help cover the cost of care at an existing off-site provider and then makes employees aware of the Dependent Care Assistance Program and Child and Dependent Care Tax Credit, which can help them further save money.

Business Costs

- Similar to benefits provided by E-commerce business Etsy, this plan involves Business B covering $4,000 of employee's child care costs. Reflecting conversations the Joint Economic Committee – Minority had with businesses providing child care benefits, this scenario involves Business B entering a contract with an existing provider and covering $4,000 of the annual average $13,184 price of child care for each participating employee.

- Calculations by the Joint Economic Committee – Minority using Census data show that 11 percent of workers in the U.S. have children under age 5. In scenario 2, we estimate that the full 11 percent of workers at this 2,500-person business use the $4,000 benefit offered by Business B, so 274 employees.
- If each of these 274 employees takes advantage of Business B's $4,000 benefit, this means that Business B spends a total of nearly $1.1 million each year on child care.

Business Savings

Like in Scenario 1, the Committee assumes that Business B employees are in a household with one child and no other working parent.

- Under the 45F program, **Business B can lower the amount of taxes it owes each year by 40 percent of the $1.1 million it spends on child care, which works out to nearly $440,000 in tax savings each year.**
- Assuming again that Business B sees the $2.90 average return-on-investment from employer-sponsored child care, this company's $1.1 million investment in child care for its employees each year would yield approximately **$3.2 million in annual** savings from reduced employee turnover and increased productivity.

Family Child Care Savings

- **Before using other tax cuts, individual employees save $4,000 per year on the total cost of child care than they would have otherwise paid.** So instead of paying the annual average child care price of $13,184, each employee pays $9,184.
- Next, as in Scenario 1, each employee sets-aside nearly $1,350 of pre-tax income each year to Business B's DCAP accounts, **meaning the employees will now pay $400 less in taxes compared to if they did not use a DCAP account.**
- Families can get a tax cut based on a portion of their remaining child care expenses through the Child and Dependent Care Tax Credit. Like in Scenario 1, a middle-income family with one child and remaining child care expenses greater than $3,000 can **lower the amount they pay in taxes by an additional $1,050 each year.**

Thus, in total, Business B saves $440,000 and an employee at the business saves $5,450 each year.

Employer-Provided Child Care Success Stories

Outdoor apparel brand Patagonia has provided on-site child care since 1983. They find:

- ✓ 100 percent of new mothers return to work.
- ✓ 25 percent lower turnover among employees using the on-site child care center compared to company-wide turnover.

Steamboat Springs ski resort built a near-site child care facility in response to its community's child care shortage and offers a 20 percent tuition discount for employees. They find:

- ✓ 90 percent of working parents intend to be working at Steamboat in a year.
- ✓ 13 avoided absences per year per parent.
- ✓ 70% of working parents say child care benefits helped them stay in the workforce.

E-commerce company Etsy provides up to $4,000 a year in child care credits to be used at a contracted provider with on-site or at-home services. They find:

- ✓ 82 percent employees said the benefit was an important factor in choosing their employer.