

**Subject** Conformity to the federal expansion of the exclusion from gross income for dependent care assistance

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## Summary

H.F. 4321 adopts a recent change in federal tax rules governing dependent care assistance that was enacted in the One Big Beautiful Bill Act (OBBBA). Dependent care assistance covers dependent care flex spending accounts and employer-provided dependent care. OBBBA increased the amount of dependent care assistance excluded from gross income from \$5,000 to \$7,500, and H.F. 4321 would adopt this increase for the purpose of the state income tax.

## Background on dependent care assistance programs

Section 129 of the Internal Revenue Code allows an exclusion from gross income for dependent care assistance that employers provide to their employees. To qualify for the exclusion, the assistance must be provided as part of a written plan for a dependent care assistance program, the requirements for which are specified in federal law. The program relies on the following definitions:

- To qualify as “**dependent care assistance**,” the employer must either pay for an employee’s “employment-related expenses” or directly provide the employee with services that would qualify as employment-related expenses.
- “**Employment related expenses**,” are certain care-related expenses associated with a “qualifying individual” that enable the taxpayer to work. The expenses may be for household services (provided that they relate to the care of the qualifying individual) or expenses for the care of a qualifying individual.
- A “**qualifying individual**” is the individual for whom care is provided. There are three categories of qualifying individuals under federal law.
  - 1) A dependent that is 12 or younger.
  - 2) A dependent who is physically or mentally incapable of caring for himself or herself and who resides with the taxpayer for more than half the year.
  - 3) The spouse of the taxpayer, if the spouse is physically or mentally incapable of caring for himself or herself and resides with the taxpayer for more than half the year.

## Limitations on dependent care assistance programs under federal law

Prior to tax year 2026, the amount of dependent care assistance that was excluded from gross income was \$5,000. The federal One Big Beautiful Bill Act (OBBBA) of 2026 increased this limit to \$7,500, effective for tax year 2026. The limit is not indexed for inflation.

The amount contributed to a dependent care assistance program also reduces the amount of expenses a taxpayer may use to claim the dependent care credit.



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