

## § 1.21-2

## 26 CFR Ch. I (4-1-23 Edition)

(2) *Cost of maintaining a household.* (i) Except as provided in paragraph (h)(2)(ii) of this section, for purposes of this section, the term *cost of maintaining a household* has the same meaning as in § 1.2-2(d) without regard to the last sentence thereof.

(ii) The cost of maintaining a household does not include the value of services performed in the household by the taxpayer or by a qualifying individual described in paragraph (b) of this section or any expense paid or reimbursed by another person.

(3) *Monthly proration of annual costs.* In determining the cost of maintaining a household for a period of less than a taxable year, the cost for the entire taxable year must be prorated on the basis of the number of calendar months within that period. A period of less than a calendar month is treated as a full calendar month.

(4) *Two or more families.* If two or more families occupy living quarters in common, each of the families is treated as maintaining a separate household. A taxpayer is maintaining a household if the taxpayer provides more than one-half of the cost of maintaining the separate household. For example, if two unrelated taxpayers with their respective children occupy living quarters in common and each taxpayer pays more than one-half of the household costs for each respective family, each taxpayer is treated as maintaining a household.

(i) Reserved.

(j) *Expenses qualifying as medical expenses—(1) In general.* A taxpayer may not take an amount into account as both an employment-related expense under section 21 and an expense for medical care under section 213.

(2) *Examples.* The provisions of this paragraph (j) are illustrated by the following examples:

*Example 1.* S has \$6,500 of employment-related expenses for the care of his child who is physically incapable of self-care. The expenses are for services performed in S's household that also qualify as expenses for medical care under section 213. Of the total expenses, S may take into account \$3,000 under section 21. S may deduct the balance of the expenses, or \$3,500, as expenses for medical care under section 213 to the extent the expenses exceed 7.5 percent of S's adjusted gross income.

*Example 2.* The facts are the same as in *Example 1*, however, S first takes into account the \$6,500 of expenses under section 213. S deducts \$500 as an expense for medical care, which is the amount by which the expenses exceed 7.5 percent of his adjusted gross income. S may not take into account the \$6,000 balance as employment-related expenses under section 21, because he has taken the full amount of the expenses into account in computing the amount deductible under section 213.

(k) *Substantiation.* A taxpayer claiming a credit for employment-related expenses must maintain adequate records or other sufficient evidence to substantiate the expenses in accordance with section 6001 and the regulations thereunder.

(l) *Effective/applicability date.* This section and §§ 1.21-2 through 1.21-4 apply to taxable years ending after August 14, 2007.

[T.D. 9354, 72 FR 45341, Aug. 14, 2007]

### § 1.21-2 Limitations on amount creditable.

(a) *Annual dollar limitation.* (1) The amount of employment-related expenses that may be taken into account under § 1.21-1(a) for any taxable year cannot exceed—

(i) \$2,400 (\$3,000 for taxable years beginning after December 31, 2002, and before January 1, 2011) if there is one qualifying individual with respect to the taxpayer at any time during the taxable year; or

(ii) \$4,800 (\$6,000 for taxable years beginning after December 31, 2002, and before January 1, 2011) if there are two or more qualifying individuals with respect to the taxpayer at any time during the taxable year.

(2) The amount determined under paragraph (a)(1) of this section is reduced by the aggregate amount excludable from gross income under section 129 for the taxable year.

(3) A taxpayer may take into account the total amount of employment-related expenses that do not exceed the annual dollar limitation although the amount of employment-related expenses attributable to one qualifying individual is disproportionate to the total employment-related expenses. For example, a taxpayer with expenses

in 2007 of \$4,000 for one qualifying individual and \$1,500 for a second qualifying individual may take into account the full \$5,500.

(4) A taxpayer is not required to prorate the annual dollar limitation if a qualifying individual ceases to qualify (for example, by turning age 13) during the taxable year. However, the taxpayer may take into account only amounts that qualify as employment-related expenses before the disqualifying event. See also § 1.21-1(b)(6).

(b) *Earned income limitation*—(1) *In general.* The amount of employment-related expenses that may be taken into account under section 21 for any taxable year cannot exceed—

(i) For a taxpayer who is not married at the close of the taxable year, the taxpayer's earned income for the taxable year; or

(ii) For a taxpayer who is married at the close of the taxable year, the lesser of the taxpayer's earned income or the earned income of the taxpayer's spouse for the taxable year.

(2) *Determination of spouse.* For purposes of this paragraph (b), a taxpayer must take into account only the earned income of a spouse to whom the taxpayer is married at the close of the taxable year. The spouse's earned income for the entire taxable year is taken into account, however, even though the taxpayer and the spouse were married for only part of the taxable year. The taxpayer is not required to take into account the earned income of a spouse who died or was divorced or separated from the taxpayer during the taxable year. See § 1.21-3(b) for rules providing that certain married taxpayers legally separated or living apart are treated as not married.

(3) *Definition of earned income.* For purposes of this section, the term *earned income* has the same meaning as in section 32(c)(2) and the regulations thereunder.

(4) *Attribution of earned income to student or incapacitated spouse.* (i) For purposes of this section, a spouse is deemed, for each month during which the spouse is a full-time student or is a qualifying individual described in § 1.21-1(b)(1)(iii) or (b)(2)(iii), to be gainfully employed and to have earned income of not less than—

(A) \$200 (\$250 for taxable years beginning after December 31, 2002, and before January 1, 2011) if there is one qualifying individual with respect to the taxpayer at any time during the taxable year; or

(B) \$400 (\$500 for taxable years beginning after December 31, 2002, and before January 1, 2011) if there are two or more qualifying individuals with respect to the taxpayer at any time during the taxable year.

(ii) For purposes of this paragraph (b)(4), a full-time student is an individual who, during each of 5 calendar months of the taxpayer's taxable year, is enrolled as a student for the number of course hours considered to be a full-time course of study at an educational organization as defined in section 170(b)(1)(A)(ii). The enrollment for 5 calendar months need not be consecutive.

(iii) Earned income may be attributed under this paragraph (b)(4), in the case of any husband and wife, to only one spouse in any month.

(c) *Examples.* The provisions of this section are illustrated by the following examples:

*Example 1.* In 2007, T, who is married to U, pays employment-related expenses of \$5,000 for the care of one qualifying individual. T's earned income for the taxable year is \$40,000 and her husband's earned income is \$2,000. T did not exclude any dependent care assistance under section 129. Under paragraph (b)(1) of this section, T may take into account under section 21 only the amount of employment-related expenses that does not exceed the lesser of her earned income or the earned income of U, or \$2,000.

*Example 2.* The facts are the same as in *Example 1* except that U is a full-time student at an educational organization within the meaning of section 170(b)(1)(A)(ii) for 9 months of the taxable year and has no earned income. Under paragraph (b)(4) of this section, U is deemed to have earned income of \$2,250. T may take into account \$2,250 of employment-related expenses under section 21.

*Example 3.* For all of 2007, V is a full-time student and W, V's husband, is an individual who is incapable of self-care (as defined in § 1.21-1(b)(1)(iii)). V and W have no earned income and pay expenses of \$5,000 for W's care. Under paragraph (b)(4) of this section, either V or W may be deemed to have \$3,000 of earned income. However, earned income may be attributed to only one spouse under paragraph (b)(4)(iii) of this section. Under the

### § 1.21-3

### 26 CFR Ch. I (4-1-23 Edition)

limitation in paragraph (b)(1)(ii) of this section, the lesser of V's and W's earned income is zero. V and W may not take the expenses into account under section 21.

(d) *Cross-reference.* For an additional limitation on the credit under section 21, see section 26.

[T.D. 9354, 72 FR 45341, Aug. 14, 2007]

#### § 1.21-3 Special rules applicable to married taxpayers.

(a) *Joint return requirement.* No credit is allowed under section 21 for taxpayers who are married (within the meaning of section 7703 and the regulations thereunder) at the close of the taxable year unless the taxpayer and spouse file a joint return for the taxable year. See section 6013 and the regulations thereunder relating to joint returns of income tax by husband and wife.

(b) *Taxpayers treated as not married.* The requirements of paragraph (a) of this section do not apply to a taxpayer who is legally separated under a decree of divorce or separate maintenance or who is treated as not married under section 7703(b) and the regulations thereunder (relating to certain married taxpayers living apart). A taxpayer who is treated as not married under this paragraph (b) is not required to take into account the earned income of the taxpayer's spouse for purposes of applying the earned income limitation on the amount of employment-related expenses under § 1.21-2(b).

(c) *Death of married taxpayer.* If a married taxpayer dies during the taxable year and the survivor may make a joint return with respect to the deceased spouse under section 6013(a)(3), the credit is allowed for the year only if a joint return is made. If, however, the surviving spouse remarries before the end of the taxable year in which the deceased spouse dies, a credit may be allowed on the decedent spouse's separate return.

[T.D. 9354, 72 FR 45341, Aug. 14, 2007]

#### § 1.21-4 Payments to certain related individuals.

(a) *In general.* A credit is not allowed under section 21 for any amount paid by the taxpayer to an individual—

(1) For whom a deduction under section 151(c) (relating to deductions for personal exemptions for dependents) is allowable either to the taxpayer or the taxpayer's spouse for the taxable year;

(2) Who is a child of the taxpayer (within the meaning of section 152(f)(1) for taxable years beginning after December 31, 2004, and section 151(c)(3) for taxable years beginning before January 1, 2005) and is under age 19 at the close of the taxable year;

(3) Who is the spouse of the taxpayer at any time during the taxable year; or

(4) Who is the parent of the taxpayer's child who is a qualifying individual described in § 1.21-1(b)(1)(i) or (b)(2)(i).

(b) *Payments to partnerships or other entities.* In general, paragraph (a) of this section does not apply to services performed by partnerships or other entities. If, however, the partnership or other entity is established or maintained primarily to avoid the application of paragraph (a) of this section to permit the taxpayer to claim the credit, for purposes of section 21, the payments of employment-related expenses are treated as made directly to each partner or owner in proportion to that partner's or owner's ownership interest. Whether a partnership or other entity is established or maintained to avoid the application of paragraph (a) of this section is determined based on the facts and circumstances, including whether the partnership or other entity is established for the primary purpose of caring for the taxpayer's qualifying individual or providing household services to the taxpayer.

(c) *Examples.* The provisions of this section are illustrated by the following examples:

*Example 1.* During 2007, X pays \$5,000 to her mother for the care of X's 5-year old child who is a qualifying individual. The expenses otherwise qualify as employment-related expenses. X's mother is not her dependent. X may take into account under section 21 the amounts paid to her mother for the care of X's child.

*Example 2.* Y is divorced and has custody of his 5-year old child, who is a qualifying individual. Y pays \$6,000 during 2007 to Z, who is his ex-wife and the child's mother, for the care of the child. The expenses otherwise qualify as employment-related expenses. Under paragraph (a)(4) of this section, Y may