Wage and Tax Considerations for Hiring Child Care Providers in Your Home

What to know if you're thinking about hiring an in-home child care provider.

Child care centers are a great solution for many working families, but they're not the right fit for everyone. Some families want more flexibility with their child care arrangement that can't be met with licensed care and/or more involvement with their child care provider. That's why they may choose to hire an in-home child care provider.

In-home child care providers are those who are not required to be licensed by the state. A private nanny is one of the most common examples of a childcare provider that is not required to be licensed, but there are others. In California, license-exempt child care providers include:

- A provider who cares only for their relatives;
- A provider who only cares for the children of only one family other than their own;
- Certain cooperative (co-op) agreements formed by parents to share child care responsibilities; and
- Certain before- and after-school programs run by schools.

This resource will focus on the child care providers that you hire to work in your home, such as a private nanny or someone in a similar role.

While your hired in-home caregiver is exempt from state licensing requirements, you, as the employer, are not exempt from local and state employment laws. It's important to be aware of these laws and comply with them to avoid penalties and other issues as you focus on safe care for your children. Here's what you need to know about hiring and paying an in-home child care provider.

Employee or Contractor?

Employers and contractors are treated very differently under both federal and state law. If you have an employee, you must withhold income taxes, Social Security, and Medicare from wages paid and you are responsible for paying taxes on those employees yourself. Contractors, meanwhile, are considered independent business people and are responsible for their own employment taxes and leave the employer with fewer legal and financial obligations – which is why it can be appealing to think of your child care provider as a contractor.

If you are hiring someone to provide care for your children, it's highly unlikely that you are hiring a contractor. Household employees are **almost always employees, not contractors**.

However, the decision is not up to you or your nanny/babysitter; there are certain rules that determine whether or not the person you hire is your employee.

In California, the basic test for determining whether you have hired a contractor or an employee is whether you (as the employer) have the right to control the manner and means by which the work is performed. In general, if the employer can instruct and/or supervise the worker and if the worker can quit or be discharged at any time, they should be classified as an employee and not a contractor.

When you are hiring an in-home caregiver, setting clear expectations upfront is vital. If someone is working with your children or other family members who may need supervision, you should clearly communicate the systems and structures you expect them to follow. This information will help set the hired in-home caregiver up for success – and is one of the key factors in determining their status as an employee, not a contractor. As the IRS explains, household workers are your employees if you can control not only the work, they do but also how they do it and clearly, the level of direction you need to provide for the care of your children falls into an employer/employee relationship.

Worker misclassification is serious business: it is considered a form of tax evasion and classifying an employee as an independent contractor in order to avoid taxes is a felony that can result in up to five years in prison and $100,000 in fines. California also allows civil penalties against employers who misclassify workers, with fines that can range from $5,000 to $15,000 per violation, with additional fines if the courts find that there is a pattern of willful misclassification. As you can see, trying to pass a household employee off as a contractor is simply not worth the risk.

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Can my hired in-home caregiver ever be considered an independent contractor? It's rare, but there are cases where your caregiver may be eligible to be an independent contractor, with wages reported on Form 1099. This **may** be the case if you hire the caregiver through an agency or if the caregiver is self-employed and runs their own business.

The IRS does a have a form – SS-8 – that can be filed by either an employee or an employer to determine a worker's status. The form asks for details on the behavioral and financial control, services provided, relationship of employer and employee, and more. If you file Form SS-8, the IRS will ask your hired caregiver to file the form, too, and vice-versa. The IRS will send a letter when the review is complete, which can take up to six months.

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Paying Wages

Once you've found the perfect in-home caregiver to hire, it's time to talk money. When determining how much to pay your in-home child care professional, it's important to remember that they are a professional and deserve to be compensated as such. That means you should be paying them a living wage and be prepared to pay taxes on their employment and offer them benefits.

When deciding how much to pay your hired caregiver, the first thing to consider is minimum wage in your area. In California, the minimum wage state-wide is $15.50 per hour, but many cities and counties have set minimum wage rates that are higher than the state. In San Francisco, for example, the minimum wage is $18.07 an hour and in Los Angeles, the minimum wage is $16.78 an hour. UC Berkeley maintains a list of current minimum wages across the state by city and county that you can refer to in order to make sure you are meeting the minimum wage laws for your area.

Minimum wage is important, but it's not the only factor to consider when determining how much to pay your hired caregiver since it may not actually be a living wage – a wage that is sufficient for maintaining a normal standard of living in your area. MIT has an online calculator that allows you to see what the living wage is for your area. The difference can be significant. For example, in Sacramento, the minimum wage is $15.50 an hour, but the living wage is $19.06 without children.

You also should consider the typical pay rates for license exempt child care providers in your area, which you can find online at sites like Indeed and SitterCity. Even if you pay a living wage, it needs to be competitive with other jobs in your community to attract the nanny you want.

Other factors to consider when determining how much to pay your hired in-home caregiver:

- Years of experience;
- Relevant education or degrees;
- Licenses and certifications;
- Number of children in their care; and
- Any additional responsibilities/chores.

Compensation Considerations

Salary or Hourly?

You may be considering paying your hired in-home caregiver a yearly salary rather than an hourly rate. Keep in mind, however, that the Fair Labor Standards Act says that domestic workers (those who provide direct or indirect care services in a private household) are entitled to overtime pay based on their hourly rate. So, you can set an annual salary for your caregiver, but doing so does not make them exempt from overtime pay. You will have to calculate their hourly rate and use that as the basis for any overtime they work.

The Fair Labor Standards Act requires you to pay your caregiver that does not live in the home with you 1.5 times their hourly rate for any hours they work beyond 40 hours a week. In California, the laws go further: the Domestic Worker Bill of Rights in California states that live in caregivers are entitled to overtime pay equal to 1.5 times their hourly rate if they work more than 9 hours a day or 45 hours a week. California also is one of the few states that mandates overtime pay for live-in caregivers.

Paid Leave

California also has a Paid Sick Leave (PSL) law, which requires that you, as a household employer, provide up to 48 hours of paid sick leave per year, with one hour accrued for every 30 hours worked. You can limit usage of sick time to 24 hours per year. Some localities throughout the state have their own rules regarding sick time, too. In Los Angeles, for example, employers can offer no less than 48 hours of sick time upfront or using the system where they accrue over time. If sick time is accrued, you must allow your employee to carry it over from one year to the next, but accrual can be capped at a minimum of 72 hours. You also can cap the use of sick time at 48 hours per year. Employers are required to comply with both state and local laws and have to provide whichever benefit is most generous to their employees.

Each pay stub or similar document must show how many days or hours of sick leave their employee has available needs to be issued the same day as their paycheck. You are not required to offer paid vacation time to your hired in-home caregiver, but if you do offer it, it's important to know that the state of California treats earned vacation time as wages that must be paid out if it is unused when employment is terminated.

The state of California has additional requirements for employers, including household employers. You are required to display/share state employment posters with your employees; some cities have a similar requirement, too. California also requires household employers to provide their hired in-home caregivers with a written notice of wages when they are hired. Your household employee must sign two copies of this notice: one for their records and one for yours. You are not required to provide your hired in-home employee with a written contract detailing the terms of their employment, but doing so is strongly suggested. You can find sample contracts online. You are required to provide your household employee with a Change in Relationship Notice if they are fired or laid off, and you are required to keep wage records on file for at least three years.

Taxes

You may be tempted to pay your hired in-home caregiver under the table, which means paying them entirely off the record, likely in cash and without withholding any taxes and without reporting them to the state or federal government. After all, this means more money for you and your employee, right? Maybe – but it could also mean big trouble for both of you. We already discussed how misclassifying your hired in-home caregiver as a contractor is considered tax evasion and can lead to significant penalties. Paying your employees under the table for the purpose of tax evasion also is illegal. It can lead to significant penalties for you and can hurt your employee, as they won't have a record of income if they need to apply for a credit card, a lease, or a mortgage. They also won't be eligible for unemployment benefits if the need arises.

So, now we know that your employee is, in fact, your employee. And if you pay those employees $2,600 or more in a year or $1,000 or more in a quarter, those employees come with tax requirements.

Before you can withhold and pay taxes, however, you'll need federal and state tax ID numbers. You can apply for a federal Employee Identification Number (EIN) from the IRS and then use that number to register with the California Employment Development Department, where you will receive a state identification number. The EIN is like a social security number for an employer – it gives an identifier for the government to track your tax contributions.

You'll also need to register your new employee with the state of California within 20 days of hiring them. Your hired in-home caregiver will need to fill out an I-9 (to verify that they are eligible to work in the United States), a federal W-4 form, and an Employee's Withholding Allowance Certificate for the Employee Development Department for the state of California. These are important records so make sure you keep at least two copies, at least one being a digital version (but know this can be as simple as taking a photo of the forms on a phone backed up to the cloud).

Now, about those tax requirements we mentioned. You may have heard of something called the "nanny tax," which is a combination of taxes withheld from the employee and taxes paid by the household employer. The nanny tax is detailed in IRS Publication 926, Household Employer's Tax Guide. In short, if you pay cash wages of $2,600 or more to any one household employee, you are responsible for social security and Medicare taxes equal to 15.3% of the employee's wages. As the employer, your share is 7.65% and the employee's share is 7.65%.

You can choose to pay your employee's share of these taxes, but if you opt not to (like most employers), you are required to withhold 6.2% of your employee's pay for social security and 1.45% for Medicare taxes. You are not required to withhold federal income taxes from wages paid to a household employee, but you can do so if the employee requests it. In addition, you are likely responsible for paying federal unemployment taxes (FUTA), which is 6% of the first $7,000 in wages paid to your household employee.

California has its own requirements for household employers, too. Household employers who pay more than $750 in wages in a quarter are required to withhold State Disability Insurance (SDI) from their employee's pay; if you pay $1,000 or more in a quarter, you also are required to pay Unemployment Insurance (UI) and Employment Training Tax (ETT). California does not require household employers to withhold Personal Income Tax (PIT), but you must report PIT wages for any hired in-home caregivers. As an employer, you also can withhold PIT if your employee requests it and you agree.

The state of California requires anyone who employs one or more full- or part-time employees to have workers' compensation insurance. In most cases, you can add workers' compensation insurance to your homeowner's insurance policy (or possibly renter's insurance if you don't own a home). Check with your current insurance provider to see if you have the option of adding workers' compensation to your homeowner's policy. If not, you'll have to purchase coverage though a workers' compensation insurance company.

You will need to supply your hired in-home caregiver with a Form W-2 by the end of January every year for their income tax purposes- it summarizes the total wages and taxes paid over the course of the previous year. And you'll need to use Schedule H (Form 1040) to determine the household employment taxes that you'll need to add to your own income tax return.

You also should consider making estimated tax payments (IRS form 1040-ES) quarterly to the federal and state government. This will help reduce your year-end tax burden and avoid an underpayment penalty from the IRS. Also California requires that household employers file an Employer of Household Worker(s) Quarterly Report of Wages and Withholding each quarter and an Annual Payroll Tax Return once a year. Do know, the federal and state deadlines don't always match up, so you'll need to track what is due when.

Whew! Sounds like a lot to keep track of, doesn't it? That's because it is. Between accurately tracking hours, wages, and taxes, handling payroll for your hired in-home caregiver can become its own full-time job. That's why many household employers in California and around the country opt for a payroll service to automate the entire process.

Taxes and Your Occasional Babysitter

If you have a babysitter you use occasionally, for a date night here and there, they likely have other clients, are working independently or with little direction, and have other characteristics that would make them a contractor and not an employee. Of course, as parents, you give specific instructions to your babysitter to follow, and they usually work an agreed upon number of hours at a time, but as a contractor, they set their own babysitting schedules, accepting or declining invitations from clients as they come up.

If you pay the babysitter more than $600 in a year, you'll want to issue a 1099 NEC, which is a tax form used in the United States to report payments made to independent contractors or freelancers. The acronym "NEC" stands for Non-Employee Compensation. The forms can be filled out online, before January 31st of the following year, then a copy is filed with the IRS. To complete the 1099 NEC, you'll need the babysitter's name, address, and Social Security number or TIN as well as the amount you paid and an employee identification number.

Your babysitter should report all their revenue, even if it is under the limit for a 1099 NEC. However, if their total babysitting revenue is less than $400 they need not report it on a tax return nor pay self-employment tax on it.

If you pay your babysitter more than $2,300 in a year or are using them on a regular, ongoing basis, they are considered a household employee and you are required to pay Social Security and Medicare taxes, as well as possibly federal and state unemployment taxes. In these cases, you should review our guidance on household employees. However, there are exceptions to this rule for babysitters who are under age 18.

Payroll

When paying your hired in-home caregiver, you should provide a pay stub that clearly states your employee's hourly rate, the number of hours worked in the pay period, gross wages, deductions taken, and net pay. One of the easiest ways to do this is to use a payroll service. Payroll services can manage, organize, and automate payments to employees in businesses of all sizes – even businesses that may have just one employee, like a household. Payroll services or software can automate the entire process of hiring and paying an employee and providing them with all of the documents they need to keep both of you in good standing with the IRS.

If you want to use a payroll service, look for one that offers:

- Automatic payroll processing;
- Tax withholding;
- Flexible pay options (such as options for paper checks or direct deposit);
- Federal AND state compliance and document submission; and
- Ability to track time worked.

If you already own a business that is structured as a sole-proprietor, or a single member LLC, S-corporation, or an LLC that files as a S-corporation, your hired in-home caregiver can be added to the payroll for that business legally to save you time and money. However, do note though an employee of your business they are still subject to all domestic worker regulations and their wages are not deductible as a business

If you do decide to use a payroll service, make sure your hired in-home caregiver knows exactly how it works – especially if they will be using it to track their time – and when and how they will be paid. There are a variety of payroll services available for household employers, including:

- SurePayroll: $49.99 per month (some tax filings may be extra); Tracks paid time off and sick leave.
- PayChex: Starts at $35 per month with extra fees for some tax services; Provides assistance for setting up new household employees.
- HomeWork Solutions: Starts at $165 per quarter for tax services and $220 a quarter for a plan that also pays your employee.

These are just a few of the payroll services currently on the market. You should be sure to carefully research any service you are interested in to make sure it fits your needs.

Benefits and Bonuses

If you do provide a written contract to your hired in-home caregiver, it should carefully detail any benefits you will offer to your employee. In deciding which benefits to offer your household employee, the first place to check is the law.

The state of California requires household employers to provide several benefits to their licensed-exempt child care providers. If your family's nanny or babysitter is asked to drive their own vehicle, you must provide a mileage reimbursement of 65.5 cents per mile (the current 2023 rate). Similarly, if they use their cell phone on the job, you should offer a reimbursement. Regulations do not specify a specific amount required, merely that the employer reimburse a "reasonable percentage," even if the employee's monthly bill does not increase from use at work.

Other Optional Benefits

Besides those benefits required for household employees by the state of California, there are other optional benefits you can consider offering. "Perks" like these show your employee that you value and respect them, their hard work, and their care of your family. Moreover, offering them as an employer makes you more attractive in the current competitive market.

Two significant benefits that employees appreciate are support with health insurance and retirement. One option for health coverage is to make contributions toward your employee's health care costs, such as their insurance premiums or co-pays. You can do this by creating individual coverage Health Reimbursement Arrangements (HRAs), an account-based plan that allows you to provide non-taxed reimbursements to employees who are enrolled in their own health insurance plan. If you decide to offer this, you must offer it to all employees who qualify. There is no minimum or maximum contribution limit for employers. If you are considering implementing an HRA or want to learn more about the variety of options available, there are a number of companies you can find to provide this service.

Another option is to purchase a health insurance plan through the Small Business Health Options Program (SHOP). SHOP plans are offered through private insurance companies, and you can decide whether to offer your employees one plan or a choice of plans, whether to offer medical, dental, or both, and how much of your employees' premiums to pay. Certain employers who use SHOP may qualify for the Health Insurance Tax Credit for Small Employers.

Contributing to your hired in-home caregiver's retirement plan is another well-received benefit. The easiest way to do this is to set up a SEP (Simplified Employee Pension) Plan or a SIMPLE IRA (Savings Incentive Match Plan for Employees). Both of these can be established online or with your financial planner in minutes and typically have no fee.

The SEP is an easy-to-implement, inexpensive retirement plan, where you can contribute up to 25% of employees' salary per year. The SEP allows you to contribute any level up to 25% in a year or none at all. All contributions are by employers, so your employee cannot use it for their savings.

A **Simple IRA** allows both employer and employee contributions. Employees can make contributions directly from their payroll up to $15,500 in 2023 (employees over 50 can contribute an additional $3,500 more). The employee contributions are pre-tax, so they don't pay tax now, but will when they withdraw the funds.

Employers must choose one of two options for their match:

- 2% nonelective contributions – this means that you must provide contributions for 2% of an employee's salary whether they save any money themselves or not.
- A one-for-one match between 1% and 3% of an employee's salary. This means that you only contribute as the employee contributes up to the maximum. The match can only be 1% for two of every five years. For example, if you offered only 1% in the first two years you would have to match at a higher rate in the third year.

You can change the amount you are contributing but you must notify employees 60 days ahead of time.

In terms of other benefits that will further distinguish you from other families hiring caregivers, consider options outside the box, like paid holidays, birthdays, offering one Friday off a month, an education or professional development reimbursement, even adding them to your gym membership.

It's also very common for families to budget for an annual bonus for their nanny or babysitter. Typically, this equals one- or two-week's salary, and it is usually given at the end of the year, around the holidays.

Final Thoughts

In-home child care is a great option for many families who want the flexibility it offers. Hiring an in-home caregiver can be complicated, though, as you are hiring an employee who you will have to manage and pay both fairly and legally. Taking the time to hire and pay this employee properly is a great way to create a relationship that starts off strong and thrives over time.

This informative resource was created for the California Child Care Resource & Referral Network by Civitas Strategies.

About the California Child Care Resource & Referral Network
The California Child Care Resource & Referral Network (Network) is a membership organization of the state-funded child care resource and referral programs in California. It addresses the needs of parents and child-care providers throughout California. The Network works with the child care resource and referral agencies in all counties in California to inform families about quality child care, to assist child care providers to serve their communities, and to encourage positive policy changes on the local, state, and federal levels. The TrustLine Registry is one of the programs administered by the Network in partnership and under contract with the California Department of Social Services (CDSS).

About Civitas Strategies
Civitas Strategies is a national management consultancy that has helped mission-driven organizations increase their impact for over 13 years. Founded in 2009 with a vision that no child grow up in poverty, Civitas Strategies' work has impacted over one million children and families collectively served by its clients. The firm's mission is to provide high-value support to help organizations become more efficient, effective, and sustainable. Today, Civitas Strategies specializes in providing training and technical assistance for the child care industry and has conducted more direct coaching and technical assistance for providers than any other organization in the US. To learn more about Civitas Strategies' services and work, visit www.civstrat.com.