Tax Related Guidance for Child Care Providers Webinar
Licensing Requirements

• Childcare providers regulated by states
• State’s licensing requirements differ
• Visit the Website for the National Resource Center for Health and Safety in Child Care and Early Education
Child Care Provider Types

• Some small family-related instances may operate without a license, but still considered a business
• In-home care provided by paid housekeeper, maid, governess, etc. - considered a household employee, reported on Sch. H
Recordkeeping

- All businesses required to maintain adequate records of income and expenses
- IRS does not dictate method, but requires records be maintained and kept
- Recordkeeping includes reasonable method of allocating costs between business and personal use
Income

- Contracts specifying charges, terms of care and responsibilities of provider and client should be kept as records
- May be formal document or informal statements reflecting rates, other considerations, and extra charges (see below)
  - Diaper charges
  - Late pick up or early drop off fees
  - Transportation costs
  - Registration fees
Income – Other Charges/Fees

• Payments for absences due to illness or vacation
• Fees to reserve position prior to coming to facility
• Days of operation and closures for holidays, vacations, bad weather days, where payment is due
Required Information Provided to Clients

- Childcare provider’s name
- Address
- Tax identification number

or may choose to use Form W-10 as alternate option
USDA
Food Reimbursement Program

The United State Department of Agriculture provides reimbursement to day care providers through the Child and Adult Care Food Program.
IRC §162: Expense

For an expense to be deductible for tax purposes by a business, per IRC §162

• Business must be for profit activity
• Expense must be ordinary and necessary
IRC §262: Personal Expense

• Only business use portion may be deductible expense, for both personal and business use
• Reasonable method of allocation must be made to determine business usage portion
• Amounts spent for personal or family reasons are **not** deductible business expenses.
Special Tax Laws

• Tax laws contain specific rules in areas where business expenses are difficult to separate from personal expenses
• Childcare industry contains many instances where there is both personal and business use
IRC §280A(c)(4) & (5)

• Provides special method for computing business use percentage of home available only for day care service providers

• Changes exclusive use provision to regular use to qualify for deduction

• Also provides limitation on deduction based on gross income
Revenue Procedure 2003-22

- Provides simplified recordkeeping requirement, optional standard meal and snack rate
- Use for calculating deductible cost of food in lieu of actual costs
IRC 280F

• Additional limitation for total amount of depreciation allowable for each year for passenger automobiles, adjusted annually for inflation

• See Publication 463, *Travel, Entertainment, Gifts and Car Expenses*
IRC §274(d)

- Must be able to substantiate certain elements of expenses for travel, entertainment, gift, transportation or listed property items such as VCRs, computers claimed as deduction

- Include:
  - Amount
  - Time
  - Place or description
  - Business purpose
  - Business relationship for some cases
Elements of Vehicle Expense

• Cost of vehicle and any improvements
• Date put in use for business purposes
• Mileage for each business use
• Total miles annually
• Date of use of vehicle
• Business destination, and
• Business purpose of expense
Vehicle Expense (Continued)

Rev. Proc. 2010-51 prohibits the use of the standard mileage rate for any automobile for which a taxpayer has claimed a deduction using a method of depreciation other than straight line, a §179 deduction, or any other additional first year depreciation.
 IRC §274(d)

Treasury Regulation 1.274-5T explains the elements in detail with examples for the four categories of expenses covered by the Internal Revenue Code 274(d).
Food Expenses

You may:

• Deduct 100% of actual cost of food consumed by your daycare recipients, or
• Use standard meal and snack rates

You may not:

• Deduct cost of food consumed by you or your family
Food Expenses (Continued)

See Publication 587, *Business Use of Your Home*, for substantiation computation for total amount deducted
- Eligibility qualifications,
- Rates, and
- Records that must be maintained
Various Supplies

• Supplies may include games, books, child proofing devices and toys.
• Most can be expensed.
• Other more expensive/longer lasting toys may need to be depreciated or expensed under IRC §179.
Business Use of Home

IRC §280A(c)(4)) qualifications:

• Be in trade or business of providing daycare for children, persons age 65 or older, or persons who are physically or mentally unable to care for themselves.

• Have applied for, been granted, or be exempt from having, a license, certification, registration, or approval as daycare center or as family or group daycare home under state law.
Business Use of Home (Continued)

• Provision changes “exclusive use” requirement to “regular use” requirement, and provides special formula for computing business percentage

• “Regular use” is portion used for business on a continuous, ongoing or recurring basis
Business Use of Home (Continued)

• Business percentage computed by multiplying space percentage and time percentage

• Space percentage consists of area regularly used for business divided by area of complete home

• Time percentage, total number of hours facility was used for childcare business during year divided by total hours in year (8,760)
Business Use of Home (Continued)

• Per IRC §280A(c)(5)), deduction for certain expenses for business use of home is limited, if gross income from business use of home is less than total business expenses

• Unallowed expenses may be carried over to next year
Depreciation

• Allows taxpayer to recover cost or other basis of certain property
• Annual allowance for wear and tear, deterioration, or obsolescence for items having useful life of one year or longer
Depreciation (Continued)

- In service in purchase year, basis for depreciation is generally cost.
- Prior to putting property in service in your business, was used for *personal purposes*, the basis for depreciation is lower of cost or fair market value on date put in service.
Depreciation (Continued)

Special provisions available to deduct cost of property faster as follows:

- IRC §179 allows some qualifying assets to have cost or part of cost expensed in year of purchase rather than depreciated
- Bonus first year depreciation or special depreciation allowances may be available for periods of time or for special areas, such as federally-declared disaster areas
Listed Property Limitations

• §179 deduction and special depreciation allowance for listed property
  – Use GDS and declining balance method, if property meets business-use requirement

• Listed property must be used predominantly (more than 50% of its total use) for qualified business use to meet requirement
Listed Property Limitations (Continued)

If property does not meet the (over 50%) rule for qualified business use then:

• It would not qualify for §179 in year placed in service, and

• It would not qualify for special depreciation allowances, including bonus depreciation
Listed Property Limitations (Continued)

• Depreciation must be figured using straight line method over ADS recovery period

• Excess depreciation on property previously used for over 50% qualified business use must be recaptured (included in income) in first year in which it is no longer used for that business percentage use
Sale of Home / Capital Gain

If home used in your business and you have a gain which qualifies for exemption from taxation under IRC §121, the portion of allowed depreciation or allowable for periods after May 6, 1997, are not tax-exempt.
Summary

- Some sources of income are unique to childcare providers; i.e. food reimbursement
- Records must be kept, including income, expense and usage records
- Various expenses and depreciation items
- Capital gain and use of home rules
IRS.gov References

Visit IRS.gov, search Keyword:

– Child Care Tax Center
– Recordkeeping
– Child Care Provider Audit Techniques Guide

• Form 8829 and instructions
IRS.gov Publications

• Publication 463, Travel, Entertainment, Gift and Car Expenses
• Publication 523, Selling Your Home
• Publication 535, Business Expenses
• Publication 583, Starting a Business and Keeping Records
• Publication 587, Business Use of Your Home
• Publication 946, How to Depreciate Property
Other Website References

• USDA.gov @
  www.fns.usda.gov/cnd/care/

• National Resource Center for Health and Safety in Child Care and Early Education @
  nrckids.org/STATES/states.htm