

Starting your day care business

You have made the decision to take on one of the most challenging activities—becoming a day care provider. Whether you care for one child, or several, it's important to keep in mind that you are operating a business and you should keep accurate income and expense records. You can operate your business in any of the following ways:

- Sole proprietorship
- Partnership
- Corporation
- Limited Liability Company (LLC)

The IRS requires an employer identification number (EIN) unless you operate as a sole proprietor with no employees. Once you have employees, the IRS requires you to obtain an EIN regardless of how you operate. For security purposes you may want to consider an EIN no matter how you operate your business.

Licensing requirements

Not all states require licensing or registration of day care providers. Some states require a license if you care for a certain number of children. Contact your state licensing authority and find out whether they require you to have a license.

Income

The fees you collect for providing day care services are taxable to you. If you are operating your business as a sole proprietor or partnership, the IRS also requires you to pay self-employment tax on your income. If you operate your business as a corporation, you are an employee of that corporation and should pay yourself a reasonable wage for the services you provide.

Customers may ask you to provide them with your social security number or EIN. This will enable them to claim the child and dependent care credit on their tax return for the amounts they pay you. They should provide you with Form W-10, Dependent Care Provider's Identification and Certification, for you to complete.

You may also receive fees from the county to assist low-income families. These are also generally taxable to you.

Claiming expenses

There are several different types of expenses that relate to a day care business that are deductible. Keep in mind that the IRS allows you to deduct all ordinary and necessary expenses incurred in conducting this activity. Some of the more common expenses are:

- Advertising
- Insurance
- Office supplies
- Legal and professional fees
- Licensing or registration fees
- Toys
- Clothing
- Diapers
- Automobile expenses. You may either deduct your actual expenses for operating your vehicle for business purposes, or you may use the standard mileage rate.
- Education and training expenses to maintain or improve your skills.
- Special equipment such as highchairs, cribs, strollers, first aid kits, etc.
- Food—either actual costs or a standard rate. (Refer to the following charts.)

Rates for July 1, 2015 – June 30, 2016			
Meals	Alaska	Hawaii	All Other States
Breakfast	\$2.11	\$1.54	\$1.32
Lunch/Dinner	\$4.02	\$2.90	\$2.48
Snack	\$1.20	\$0.86	\$0.74

Rates for July 1, 2016 – June 30, 2017			
Meals	Alaska	Hawaii	All Other States
Breakfast	\$2.09	\$1.53	\$1.31
Lunch/Dinner	\$3.99	\$2.88	\$2.46
Snack	\$1.19	\$0.86	\$0.73

As a day care provider, you may be eligible to participate in a food program administered by the Department of Agriculture. These reimbursements are taxable to the extent they exceed your food costs. If your food costs are more than your reimbursements, the difference is a deductible expense.

As with all expenses, if you are reimbursed, you must reduce your deductible costs by the reimbursement.

Business use of your home

When conducting a business activity in your home, the IRS allows you to deduct the expenses that relate to the use of that space. If you use space in your home on a regular basis for providing day care, you may be able to deduct the business expenses for that part of your home even though you personally use the same space. To qualify for this exception to the exclusive-use rule, you must meet the following requirements:

- Be in the trade or business of providing day care 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 a day care center under state law. You do not meet this requirement if your state rejected your application or revoked your license or any other authorization.

There are two methods when figuring the deduction for business use of the home: the regular method and the simplified method. For both methods you must maintain accurate records of the time spent providing care and the square footage of the rooms you use for day care on a regular basis (i.e., the time-space percentage). For the regular method, this percentage is important because it represents the proportion of your home that you use for business. Apply this percentage to the following expenses and deduct them from your income:

- Casualty losses
- Mortgage interest
- Property taxes
- Homeowner's insurance
- Rent
- Home repairs and maintenance
- Utilities
- Depreciation
- Home improvements

Formula for time-space percentage

$$\begin{aligned} & \text{Number of hours you use your home} \\ & \text{for business} \\ \div & \text{ Total hours in a year (8,760)} \\ \times & \text{ Number of square feet in home you} \\ & \text{use regularly for business} \\ \div & \text{ Total number of square feet in your home} \\ = & \text{ Time-space percentage} \end{aligned}$$

For the simplified method, if you maintain a qualifying home office, you may elect to deduct \$5 per square foot of home office space up to 300 square feet, for a deduction up to \$1,500. If you choose this method, you cannot depreciate a portion of your home; however, you can claim allowable mortgage interest, real estate taxes and casualty losses on the home as itemized deductions on Schedule A. Discuss the special income tax requirements of operating a day care with your tax professional.

This brochure contains general tax information for taxpayers. As each tax situation may be different, do not rely upon this information as your sole source of authority. Please seek professional advice for all tax situations.

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Tax Tips for Day Care Providers

