

Regular Business Expenses

Advertising: Below is a list of some of the kinds of advertising expenses that you might incur for your business: answering service; balloons; bumper stickers; business cards; business flyers and door hangers; buttons; cost of designing a business logo; cost of designing a web page; finder's fee for parents who refer another parent to your program; membership dues to your local Chamber of Commerce or other business organization; name badges; newspaper classified ads; parent newsletters; parties and picnics for parents of the children in your care; photo album or scrapbook to display photos and other information about your business during parent interviews; photographs you take of the children in your care that you share with their parents; printing and typesetting expenses for marketing materials; radio ads; registration fee to register your business name in your state; rubber stamps with your business name and return address for mailing letters; tote bags; T-shirts for the children in your care or T-shirts you wear to advertise your business; welcome mat; yard, magnetic, car and window signs; Yellow Pages listing; any other forms of business advertising.

Bad Debts: Some providers believe that if a parent leaves owing them money, they can claim this as a bad debt loss, but this is not so. The only situation in which you can claim a bad debt loss is when a parent pays you by check, you report this money as income on your tax return, and the check bounces in the next tax year. This rarely happens. If a family leaves without paying you, just don't report the money they owe you as income. As a result, you will have a lower taxable income.

Employee Benefit Programs: This refers to benefit programs for the employees you hire for your business. When you hire employees, you do not have to pay them any benefits beyond their wages. If you do offer benefits, such as health and dental care or retirement plans, however, you can claim 100% of these expenses here.

Insurance: The cost of worker's compensation insurance for yourself and your employees is 100% tax deductible. You can also deduct the cost of any family child care liability and accident insurance policy. You can also deduct the business portion of any insurance you carry on your personal property, using your time-space percentage. Renters can deduct the cost of renter's insurance on their personal property. The cost of car insurance is not deductible unless you use the actual car expense method. The cost of life insurance and disability income insurance for you is not deductible.

Interest: You may deduct the cost of interest that is charged on items you use in your business. For example, if you purchase a swing set for \$700 on your credit card, use the swing set only for business, and pay \$50 in interest for this item during the year, you can deduct the full \$50. If your own children also use the swing set, you can deduct the time-space percentage of the interest. If you can show that the swing set was used more than your time-space percentage would indicate, you can claim a higher percent of the interest.

Legal & Professional Services: Tax preparation fees to file your business tax forms are deductible as a business expense. The cost of hiring a payroll service to fill out federal and state forms for your employees is deductible. Professional assistance for your business, such as accounting, legal services and bookkeeping services, is also deductible as a business expense. Legal fees and court costs for suing a parent for nonpayment in small claims court are also 100% deductible.

Office Expenses: Below are examples of the kinds of business expenses that you can include under the category of office expenses: **Bank Charges:** You can deduct all the costs associated with keeping a separate business checking account, including the cost of printing checks. If your bank charges a per-check service fee, you may also deduct a portion of the costs of your personal checking account. If a parent's check bounces and the bank charges you a fee, ask the parent to reimburse you for the fee. If you can't reclaim this fee from the parent, you can deduct it as a business expense. **Books:** Tax publications and child care related books – such as first aid and medical emergency books – are all 100% tax deductible. This would also include all of the books that can be purchased through Books by Kelly. If you have young children of your own, your encyclopedia and children's books are only partly deductible using the time-space percentage. **Computer Related Items:** You can deduct the portion of the cost of computer software and related items based on the percent of time you use your computer for business. Deductible items may include Microsoft Word, Excel, QuickBooks, Quicken, computer disks, paper, printer cartridges and other computer supplies. You can also deduct the cost of subscriptions to online services, email and internet access fees. **Dues:** The membership fees and dues for local child care associations and organizations such as the National Association for the Education of Young Children, the National Association for Family Child Care, and Redleaf National Institute are fully deductible. Dues for membership in personal organizations such as country clubs, community centers, Sam's Club are not deductible. **Magazines:** You may deduct the cost of any magazines used in your business. For example, Sesame Street; Scholastic; Disney Magazine; Jack & Jill; Highlights for Children; Parents; Working Mother; Family Circle; Pre-K Today; etc. **Other:** In addition to the major categories listed above, there is a wide range of other items and services that can be claimed as office expenses: adding machine & tape; bulletin board; business forms; business stationary; calendar and/or planner; cellophane tape; chalkboard; correction fluid; envelopes; erasers; fax machine; file cabinets; file folders; greeting cards for the parents or their children; ledger; notebooks/notepads/folders; paper; paper clips; parent newsletters; pencils; pencil sharpener; pens; photocopying costs; pocket calculator; postage stamps; post-it notes; receipt books; stapler/staples; storage boxes; etc.

Rent of Business Property: You may deduct the cost of renting items for your business, such as videos, computer games, a carpet cleaning machine or party equipment. If your own children use these items after the other children have left, you should claim only your time-space percentage of the rental cost.

Repairs and Maintenance of Personal Property: Personal property includes all items that are not permanently attached to your home or land, such as furniture and appliances. The cost of making repairs to personal property that was damaged or worn out by your business is fully deductible. For example, if a child in your care damages your microwave or DVD player, you can deduct the full cost of the repair as a business expense. If your own child causes the damage, you could deduct only your time-space percentage of the cost. If you hire someone to clean your rugs or do your laundry (such as a cleaning service, diaper service or dry cleaner) you may deduct at least part of the cost as a business expense. Repair and maintenance expenses can include the following: carpet/rug cleaning expenses; flashlight and batteries; pest control; poison prevention stickers; recovering sofa, couch or chair; repairs of a television, VCR, DVD, computer, toaster, furniture, appliances, toys, etc; salt for water softener; service contracts on appliances.

Supplies: Arts & Crafts: Crayons; markers; poster board; paints; coloring books; art & craft supplies; paint brushes; chalk/chalkboard; clay; construction paper; glue; paper; paste; stencils; stickers; yarn; etc. **Baby:** diapers; diaper pail; baby wipes; bibs; tippy cups; changing pad; bottles; nipples; bottle/nipple brush; diaper bags; rubber gloves used for diaper changing; baby intercom/monitor system; baby swing; baby walker; booster seat; cribs/mattresses; high chair; infant seat; playpen; potty chair; stroller; car seat; etc.

Cleaning: air fresheners; bleach; broom; cleansers; clothes hamper; clothes iron; clothespins; dishwasher detergent; dust mop; dustpan; electric dust buster; fabric softener; furniture polish; Laundromat costs; pail or bucket; rubber/latex gloves; rug cleaner; scouring pads; soap; sponges; stain removers; toilet bowl cleaner; vacuum cleaner; vacuum bags; wastebasket; wet mop; window cleaner; etc. **Education:** preschool programs; books; educational video & audio cassettes; board games; flannel board; flannel board stories & accessories; puzzles; science materials; puppets; musical instruments; song books; props for pretend play; dress up clothes; etc. **Household:** any item purchased to make your home more accessible to a disabled child or parent; home decorations; candles; flashlight; bedding; towels; bath mat; bathroom scale; camping equipment; clocks; extension cords; fireplace fixtures; flowers; flower boxes; mirrors; nightlights; indoor or outdoor thermometer; shelving; sleeping bags; space heater; storage containers; telephone; tools; umbrella; sheets; window shades/blinds; wall posters; baking dishes; beater; blender; toaster; bowls; cookbooks; cookie sheets; cookie cutters; cutting board; dish towels; dishes; electric can opener; food processor; flyswatter; garbage can; glassware; knives; measuring cups & spoons mixer; popcorn popper; iron; potholders; pots & pans; serving dishes; silverware; tablecloths; Tupperware; utensils; waffle iron; charcoal; washcloths; batteries; garden hose; shovel; rake; etc. **Movies:** home videos or DVDs purchased for home viewing. **Music:** CD's or audio cassettes purchased for listening. **Paper:** Kleenex tissue; paper towels; toilet paper; garbage bags; napkins; paper cups; paper plates; plastic silverware; food storage bags; straws; aluminum foil; etc. **Safety:** safety barriers (gates); safety caps for electrical outlets; safety locks for medicine and poison; safety locks for fire arms; first-aid kits; cotton swabs; medicine; fire extinguisher; thermometer; sun screen; insect repellent; fire alarm; fire escape ladder; syrup of ipecac; etc

Taxes and Licenses: If you pay payroll taxes for your employees (Social Security, Medicare, federal unemployment, state unemployment, and so forth), you may deduct the full cost of these expenses. All fees and costs you incur to become licensed or regulated are also 100% deductible. This would include the following: background checks; fingerprinting fee; fire or health department inspection fees; licensing fees; medical exams & X-rays; recharging or testing fire extinguishers; social service department fees; tuberculosis test; water testing; zoning fees; etc. You can deduct all the sales tax you pay on business purchases (although it is easier to include this in the cost of the purchase rather than claim it separately). Your quarterly estimated income tax payments cannot be claimed as a business expense.

Travel/Lodging: If you travel away from home overnight and the primary purpose of your trip is business, you may deduct the costs associated with the trip. Such trips might include travel to a family child care conference, field trips with the children in your care, or business workshops. You may deduct the full cost of your transportation – car expenses, car rental, airplane, bus, train, taxi and so on – and lodging. Other deductible costs for overnight business travel include: hotel tips or long-distance calls to check on your business. The cost of hiring someone to care for your own children while you are away on business is not a business expense, but can be claimed toward your personal child care tax credit.

Meals & Entertainment: If you travel away from home overnight and the primary purpose of your trip is business, you may deduct 50% of your actual food and entertainment costs, or you can claim the standard meal allowance, which is \$30 per day in most areas of the United States. However, the standard meal allowance is also subject to the 50% rule, so if you use it the amount you can actually deduct for one day is \$15. You don't need any receipts to claim the standard allowance, but it doesn't cover travel to Alaska and Hawaii. Each year you must choose between actual expenses and the standard meal allowance for all your food expenses; you can not use both methods in the same year.

Telephone: The monthly cost of the first telephone line in your home is not a deductible business expense, even if the phone was only installed in order to meet regulation requirements. If you install a second phone line, you may deduct the business portion of this cost, based on the amount of time you spend on business versus personal calls. You can also deduct a portion of the cost of purchasing the phone itself. If you use a cell phone or pager for business purposes, you can deduct a portion of the monthly costs. The following telephone-related costs are all deductible: long-distance business calls; custom calling features (such as call waiting, call forwarding, caller ID and custom ringing); headset for a cordless phone; repair fees for the phone and phone lines; linebacker maintenance fees; an answering machine or service; a separate business listing in the White Pages; Yellow Pages advertising; and a TDD to receive calls from deaf parents or children.

Wages: Many providers hire assistants or substitutes to work with the children in their care. From a tax standpoint the critical question is: Are these workers your employees or are they independent contractors? The difference has major tax implications: If the workers are your employees, you must withhold Social Security and Medicare taxes and pay federal unemployment tax and the employer portion of their Social Security and Medicare tax. You will probably have to pay them the minimum wage. You may also have to withhold state and federal income taxes from the worker's wages. Your state laws may require you to pay state unemployment taxes and purchase worker's compensation insurance. If the workers are independent contractors, you do not need to withhold or pay any taxes for them. You will need to issue Form 1099 – Misc if you pay an independent contractor over \$600 in one year. Keep in mind that almost anyone who works for you, for any number of hours, will generally be considered an employee by the IRS.

Activity Expenses/Field Trips: Family childcare providers are in the business of celebrating birthdays and holidays with the children in their care. Parents will expect you to hold celebrations and parties to teach children about traditions, customs, sharing and other cultures. Therefore, the expenses of these activities, including the gifts you give to the children, are activity expenses and should be claimed as such. When you throw parties and celebrations for the children in your care (or for their parents), you can deduct the full cost of all your expenses, including food; snacks; balloons; paper tablecloths; prizes; streamers; hiring a clown or storyteller; etc. Other activity expenses might include the following: film and film developing; fees for field trips; food deliveries (such as pizza); music lessons; swim lessons; recreation center fees, movies; etc. Keep in mind that the fees paid for field trips for your own children are not a deductible expense.

Gifts: Any gifts purchased for daycare children, parents or helpers. There is a \$25.00 maximum allowance per person, per year.

Toys: Toys are deductible according to the percentage of time they are used for your business. If you have children of your own, the IRS may question whether the toys you buy are really business deductions. You can strengthen your case by saving all of the receipts for the toys you buy for your own children. Also, don't try to claim 100% of toys that are also used by your own children after business hours. The IRS *Child Care Providers Audit Techniques Guide* recognizes that toys can be a significant expense for providers and tells auditors to look for "large, unusual, questionable, and personal items."

Training/Education: The benefits of professional development in the family child care field are obvious. To the provider, it offers knowledge and skills that can enrich her career. To the child in care, it can mean a better educational environment when the provider is able to transmit the knowledge she has learned. To the parents of children in care, it can be a strong indicator of quality care. Such indicators will likely grow in importance as parents look for objective standards to help them select a caregiver for their child.

I strongly recommend that all family child care providers take every opportunity to improve their skills by enrolling in professional development classes and obtaining educational credentials such as the National Association for Family Child Care (NAFCC) accreditation, Child Development Associate (CDA), and post-secondary degrees in the early childhood field.

Deducting the Cost of Education

Although it might seem at first to be a simple matter, the question of whether or not professional development classes and credential are deductible is actually quite complicated.

Classes or workshops that you take to get ready to care for children are deductible, but classes or workshops that you are required to take by state law before you can get a state license are not deductible. So if you take a class on child development before you are licensed, it is deductible. However, if state law says that you have to have taken a class in child development before you can get licensed, then it's not deductible. IF state law says you must take 10 hours of training a year after you get licensed, then the cost of classes you take before and after you are licensed are deductible.

Any training you receive after you meet your state's child care regulations is deductible as long as the training is related to your business (not classes on chemistry or engine repair!). Such training classes are deductible even if they don't qualify for training credit according to your local regulation requirements. In other words, if you take a class on record keeping that doesn't count towards your state training requirements, this class is still deductible.

All costs associated with obtaining NAFCC accreditation or a CDA are always deductible. Education expenses related to child development, taxes, CPR, parent communication, nutrition, or any other class to increase your skills to run your business are deductible. Classes in a second language are deductible only if you use this skill to build your business or if you teach the language to children.

College Education

You cannot deduct the cost of classes you take to receive a post-secondary undergraduate degree if this is your first post-secondary degree. The reason you cannot deduct this is because the degree qualifies you for a new occupation. Such classes are not deductible even if the class helps you maintain or improve your skills as a provider.

If you take college classes that do not lead to a degree (a class on child development, for example), then they are deductible. If you already have a post-secondary degree and you are taking classes that qualify you for a second college degree (a degree in early childhood development or a masters degree in education, for example), then these classes are deductible.

Scholarships

If you receive a grant or scholarship (TEACH, etc.) to take training classes or attend business conferences, the money you receive is taxable income. But you can also deduct the cost of the conference or classes that you take. If the grant does not cover the full cost of the training, you can still deduct the full cost. If you never actually receive the scholarship (the granting organization pays for the training directly), you should still report this as income and claim the cost of the training as an expense.

Home Expenses

Home Expenses are the costs that you incur to keep and maintain your home. You can deduct the business portion (the Time/Space %) of these expenses. If you don't own a home, you may claim the business portion of any expenses paid for your living quarters, such as rent, utilities and renter's insurance.

Casualty Losses: A casualty loss is the damage, destruction or loss of property that results from an identifiable event that is sudden, unexpected or unusual, such as an earthquake, tornado, flood, storm, fire, car accident or act of vandalism. If your home or care insurance completely covers the damage you incurred, you don't have a business expense. However, if you have an insurance deductible of \$250 and you pay this amount, it is a business expense.

Mortgage Interest Paid and Real Estate Taxes: You are always entitled to claim the business percent of your mortgage interest payments and real estate taxes, even if this creates a loss for your business. You will deduct your time-space percentage of these expenses, and if you itemize deductions, you can deduct the remainder on Schedule A.

Homeowner's Insurance: You can claim the time-space percentage of home insurance (including flood insurance), which provides you with financial protection in case of damage to your home. Other kinds of insurance policies (renter's insurance, liability, medical, etc) are not included with the home expenses.

Home Repairs and Maintenance: Home repair and maintenance expenses are the costs you incur to maintain your home's present value. You can claim the time-space percentage of these expenses: asphalt repair of driveway; carpet-cleaning service; corner wall guards; cupboard latches and locks; deck staining; dehumidifier; electrical fuse replacement; floor sanding; furnace cleaning/inspection/repairs; homeowner's association dues; house-cleaning service; humidifier; lead paint removal; light fixture repair; painting the interior or exterior of the house; patching walls & floors; plumbing repairs; radon or lead testing & abatement; roof shingle repair; rubber stair treads; screen repair; tree removal/trimming; wallpapering; window repair; etc. There is a difference between home repairs and home improvements. Home repairs are expenses that you incur simply to maintain your home's present value. Home improvements are expenses that increase the value of your home or prolong its useful life; these costs must be depreciated over a number of years.

Utilities: You can claim the time-space percentage of your utility expenses, unless you can show that your business-use percent of a particular expense is higher than that. For example, if you have no children of your own and only use the Disney Channel for your business, you can claim 100% of its cost. Some examples of utility expenses: cable television; electricity; kerosene to heat the home; natural gas; oil to heat the home; propane gas to heat the home; recycling fees; satellite television; sewage disposal; trash removal; water; wood to heat the home.

Rent: If you rent your home or apartment, you can claim the time-space percentage of the rent you have paid.

House: Based on the value of your home when you started your daycare business, it will be depreciated over 39 years.

Depreciation

Depreciation – Most items that cost more than \$100 and last longer than one year gradually wear out, which means their value decreases over the years. That is why the tax laws require you to claim these items by deduction their value over time.

Section 179 – Section 179 is a special depreciation rule that allows you to write off up to \$125, 000 (2007 Rules) of personal property expenses in one year rather than depreciating them over a number of years. To use this rule you must have purchased the item in that year and you must use it more than 50% for business. If you start using the item less than 50% for business or you go out of business before the end of normal depreciation, you will have to pay taxes on part of the deduction you claimed.

Automobile: You can only claim depreciation for your car if you are using the actual expenses method, and most providers use the standard mileage rate method, which is designed to include the depreciation. According to the 2007 rules, cars must be depreciated over five years. If you start using the standard mileage rate method and switch to the actual expenses method in a later year, you can then start claiming depreciation on the car. However, the five-year depreciation period starts running the year that you first use the car for business.

Personal Property: The term *personal property* refers to items that are used in your business and are not attached to your home or land. Most providers use a significant amount of personal property for their business, and this makes it worthwhile to keep accurate records and depreciate these expenses. There are three categories of personal property and each category has different depreciation rules: computer equipment; property used for entertainment/recreation/amusement; all other personal property.

Computer Equipment: This category includes computers, printers, scanners, printer stands and computer tables. According to 2007 rules, the items in this category must be depreciated over five years. Do not use your time-space percentage for this expense category. Instead, record how much time you use your personal computer for business purposes (including children's games, business record keeping, menu planning, internet research or marketing) and how much time you use it for personal purposes. Divide the number of hours you use the computer for business by the total number of hours you use the computer to compute an actual business-use percentage.

Equipment for Entertainment, Recreation or Amusement: This category includes items such as TV's, VCR's, DVD players, video recorders, cameras, camcorders, radios, pianos & other musical instruments, video games, etc. According to the 2007 rules, the items in this category must be depreciated over seven years. Do not use your time-space percentage for these items. You must keep track of how much time you use each of these items for business in the same way described above for you computer.

All other Personal Property: The last category of personal property includes all personal property that wasn't covered in the first two categories. However, if any of these items (such as built-in appliances) are permanently attached to the home, they must be depreciated as home or home improvement items rather than personal property items. According to the 2007 rules, the items in this category must be depreciated over seven years. Some of the items in this category include: bean bag cushion; bed & headboard; bedside table; bookshelves/cases; buffet; bureau; carpet sweeper; cellular phone; chairs; changing table; chests; climbing apparatus; clothes dryer; coffee tables; couch; dehumidifier; desk; dining-room table & chairs; dishwasher; draperies/curtains/blinds; dressers; electric heating unit; end tables; entertainment center; fans; fax machine; file cabinet; fireplace hardware & screen; freezer; general furniture; grill; hand tools; jungle gym; ladder; lamps;

lawn furniture; lawn mower/spreader/sprinkler; mats; mattresses; microwave; mirrors; outdoor play equipment; outdoor shed; photocopier; picnic table; pillows; planters; playground equipment; playhouse; porch/deck furniture; power tools; refrigerator; rocking chair/recliner; rugs/carpets; sewing machine; slide; snow blower; sofa; space heater; steam cleaner; stove; stroller; swing set; tables; telephone; tiller; trash compactor; vacuum cleaner; wall decorations; wall pictures/paintings; washing machine; water softener; window air conditioner; workbench; etc.

Land Improvements: Land improvements are expenses that increase the value of your property and will remain attached to the land after you leave. If the item does not have a secondary purpose or is not attached to your home it is not deductible. Land improvements may include the following: basketball stand, build-in sandbox, cement slab, cement stairs & railings, drilling a well, fence, fence around a pool, landscaping adjacent to home, lawn sprinkler system, new driveway, patio, play equipment that is permanently attached to the land, retaining wall adjacent to the home, septic tank installation, sidewalk or walkway, sod adjacent to home, swimming pool, trees/shrubs/bushes adjacent to home, water/well pump, wood chips for outdoor play equipment.

Home Improvements: Home improvements are expenses for permanent improvements or modifications that increase the value or prolong the useful life of your home. Don't confuse home repairs with home improvements. A repair (such as painting or fixing a broken pipe) merely protects or maintains the current value of your home. According to 2007 rules, home improvements must be depreciated over 39 years. Home improvements may include the following: acoustical ceiling tiles; architect fees; attic fan; awnings; built-in appliances; built-in cabinets/bookshelves; built-in mirrors; carport; ceiling fan/replacement; central air conditioning; central cleaning system; chimney damper; circuit breaker; closet shelves; cupboards; deck; doorbell; doors/replacement; duct work; fireplace/heater insert; fireplace/mantel; floodlights; furnace; fuse box; garage; garage door opener/replacement; garbage disposal; gutters & drain pipes; insulation; intercom system; kitchen countertop; lawn sprinkler system; mailbox; new plumbing or electrical to bring house up to code; new room addition; paneling; patio & cover; permanent light fixture; porch; remodel of kitchen/bathroom; replacement screens; replacement windows; screen doors; security locks; security system; shed; siding; storm or screen windows; water filtration system; waterproofing; weather stripping; wired-in smoke detectors; etc

Home: Your home is probably the most expensive item you will depreciate, and therefore it requires special attention. You will always be better off financially if you depreciate your home. There are two important reasons for taking depreciation on your home. By taking depreciation on your home, you will probably reduce your taxable income by hundreds of dollars every year you are in business. The depreciation you claim on your home is subject to taxes when you sell it, and the IRS rules state that if you are entitled to claim home depreciation, you will be treated as though you did claim it. This means that you will have to pay tax on this amount even if you didn't claim it.