### Michigan's Child Care Stabilization Grant and Taxes

A Webinar for Home-Based Child Care Providers

### This webinar was made possible thanks to the Michigan ECE Community of Practice Team:

Members include representatives from BC Pulse, BUILD Initiative, Detroit Hispanic Development Corporation, Early Childhood Investment Corporation, Early Learning Neighborhood Collaborative, First Steps Kent, Grand Rapids Chamber, Hope Starts Here, KC Ready 4's, M.A.C. Tax Service, Michigan's Children, Refugee Education Center, Southeast Michigan Early Funders Collaborative, The Grand Rapids Early Discovery Center, YWCA Kalamazoo, and Vibrant Futures.

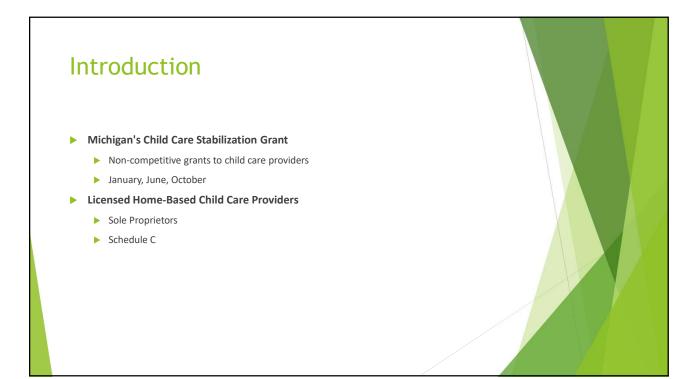


### Special Guest

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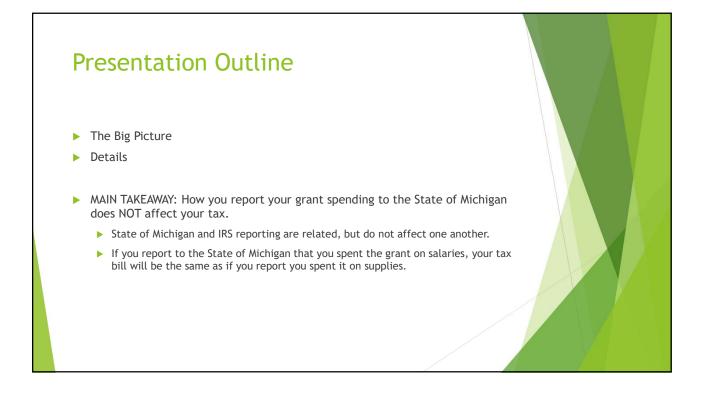
### Introduction

### Informational Only

- > This webinar has been prepared for informational purposes only.
- The impact of the funding will vary from provider to provider, and this webinar is not intended to provide, and should not be relied on for tax, legal, or accounting advice.
- You should consult your own tax, legal, and accounting advisors before engaging in any financial transaction.

### Questions?

- Please put questions in the chat.
- > Answers will be provided throughout the presentation and at the end.



### The Big Picture

### Are grants taxable income?

- Child Care Stabilization Grants are taxable income.
- > Taxable on federal, state, and local levels.

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### Consulting your tax advisor

- Call the person who prepared your 2021 tax return.
- Tell that tax preparer how much grant income you will receive during calendar year 2022.
- Answer the tax preparer's questions.
- That tax preparer will give you the most accurate answer about how much tax will be due.
- ▶ If your 2021 tax preparer cannot tell you, contact a different tax professional.
- A tax preparer may or may not charge for time spent giving you advice.
- Cost of business tax preparation is tax deductible and good tax advice will likely save you money on taxes.

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### Allowable Expenses and Taxable Income

- Gross Income: All business income for the year
- > Child Care Expenses: Child care-only expenses
- **Shared Expenses:** Expenses with both child care and personal use
- Time-Space Percentage: Your business-use-of-home percentage which is calculated based on your square footage and child care hours
- Net Profit: Gross Income Child care Expenses (Time-Space Percentage x Shared Expenses) = Net Profit

Net Profit = Taxable Income

As a business owner, you are taxed on your net profit!

### Allowable Expenses and Taxable Income

- For tax purposes, grant income is treated the same as any other type of income.
- For tax purposes, allowable grant expenses are treated the same as any other type of expenses.
- Normal Expenses: Expenses you pay for every year for your child care business
  - Supplies, food, business insurance, business miles, utilities, mortgage, etc.
- **Extra Expenses:** Expenses you would not incur without the grant
  - Bonuses paid to employees (not yourself), shared expenses you would not purchase unless you received the grant income, etc.

### Allowable Expenses and Taxable Income

- All of the examples that follow assume:
  - ▶ 30% time/space percentage
  - 33% total tax rate
    - Social Security + Medicare + federal income tax + state income tax + local income tax
  - \$30,000 in grant income during 2022
- Your time/space and tax rate are different than these examples!
- > Your tax advisor can help you determine these.

### Extra Child Care-Only Expenses and Taxable Income

### Without Grant Income

2022 Gross Income \$50,000 2022 Child Care Expenses \$10,000 2022 Shared Expenses \$10,000

### With Grant Income

2022 Gross Income \$80,000 2022 Child Care Expenses \$40,000 2022 Shared Expenses \$10,000

Net Profit \$50,000 - \$10,000 - (.3 x \$10,000) = \$37,000 Net Profit \$80,000 - \$40,000 - (.3 x \$10,000) = \$37,000

Tax Calculation **\$37,000 x .33 = \$12,210** 

Tax Calculation \$37,000 x .33 = \$12,210

In this example, the tax on \$30,000 in grant income is \$0 (0%).

### Extra Shared Expenses and Taxable Income

### Without Grant Income

2022 Gross Income \$50,000 2022 Child Care Expenses \$10,000 2022 Shared Expenses \$10,000 With Grant Income

2022 Gross Income \$80,000

Net Profit \$50,000 - \$10,000 - (.3 x \$10,000) = \$37,000

Tax Calculation \$37,000 x .33 = \$12,210

2022 Child Care Expenses \$10,000 2022 Shared Expenses \$40,000

Net Profit \$80,000 - \$10,000 - (.3 x \$40,000) = \$58,000

Tax Calculation \$58,000 x .33 = \$19,140

In this example, the tax on \$30,000 in grant income is \$6,930 (23.1%).

### Normal Expenses and Taxable Income

### Without Grant Income

 2022 Gross Income
 \$50,000

 2022 Child Care Expenses
 \$10,000

 2022 Shared Expenses
 \$10,000

### With Grant Income

 2022 Gross Income
 \$80,000

 2022 Child Care Expenses
 \$10,000

 2022 Shared Expenses
 \$10,000

Net Profit \$50,000 - \$10,000 - (.3 x \$10,000) = \$37,000

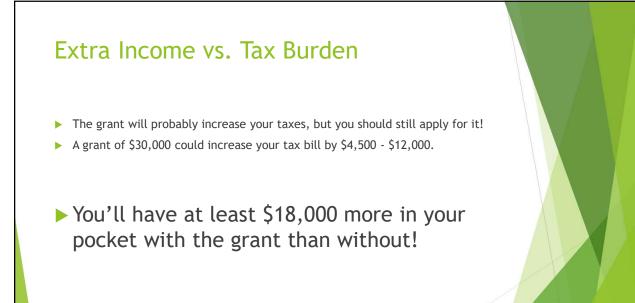
\$80,000 - \$10,000 - (.3 x \$10,000) = \$67,000

Tax Calculation **\$37,000 x .33 = \$12,210** 

Tax Calculation **\$67,000 x .33 = \$22,110** 

In this example, the tax on \$30,000 in grant income is \$9,900 (33%).

Net Profit



### Grants and Government Benefits Eligibility for some government benefits may be income-based Medicaid

- CHIP
- Pell grant or other financial aid
- Section 8 housing voucher
- Social Security or SSDI benefits before full retirement age
- ACA health insurance subsidy (Obamacare / Marketplace health insurance)
- SNAP
- ► TANF
- Great Start Readiness Preschool
- Child care assistance
- Free school lunch
- Utility bill assistance / home heating credit / Affordable Connectivity Program (internet)

### Grants and Government Benefits

- If you gualify for these or other income-contingent benefits:
  - First, contact your 2021 tax preparer, explain your 2022 grant income and ask for an estimate for what your total income and AGI will be for 2022.
  - Then, contact your case manager/insurance agent/financial aid office/school district/etc. to ask how your changed income will affect your eligibility for a government benefit. Do this before applying for the Summer grant so that there are no surprises.
- You can then determine if the benefit of the grant income will outweigh the cost.
- With advance planning, you may be able find ways to spend much of the grant income to improve your child care without increasing your net income and government benefit eligibility.

### Preparing for Taxes

- Not sure if your expenses are normal or extra? Assume they are normal and that your tax burden will increase.
- > You can *plan ahead* so the tax increase does not cause hardship.
- CHOICE 1: SAVE
  - > Ask your 2021 tax preparer how much to save and set that amount aside for taxes.
  - ▶ OR set aside 40% of the grant money for taxes.
  - When you file your return, you can use this saved money as necessary to pay your tax obligation and keep the rest.
- CHOICE 2: ESTIMATED TAX PAYMENTS
  - Make or increase your quarterly estimated tax payments in advance of filing your return.
  - Consult your tax preparer about how to do this.



### Form 1099-NEC

- ▶ Form 1099-NEC reports non-employee compensation.
- You will receive Form 1099-NEC from the State of Michigan in January or February of 2023.
- Form 1099-NEC will be delivered to you either by mail or online.
- SOM will also send a copy to the IRS.
- Form 1099-NEC may combine your grant income with any CDC subsidies you received.
- If you think the 1099-NEC you received was wrong:
  - First, check your bank records to confirm.
  - > Next, contact the State of Michigan to request an explanation or correction.

### Grant Reporting vs. Tax Reporting

### **Grant Reporting**

 Use the method and categories required by the State of Michigan.

### Tax Reporting

- Report grant expenses in the same way as any other expenses.
- Do not separate expenses paid for with grant income from expenses paid for with other income.
- For example, if you use \$2,000 in grant income for supplies and \$500 in other money for supplies, you would simply report \$2,500 in supplies expense on your tax return.

### When to Report Income and Expenses

- Most child care providers are cash-basis taxpayers.
- Cash-basis taxpayers report:
  - Income in the year they receive it
  - > Expenses in the year they pay for those expenses
- Keep this in mind if you will spend your grant income in a different year than you receive it.

### Employee Bonuses

- You will not pay income tax on grant money that you use to pay a bonus to an employee (not yourself).
- The extra expense (the bonus) will cancel out the extra income from the grant.
- \$1,000 income (grant) \$1000 extra expense (employee bonus) =
  - ▶ \$0 taxable income
  - ▶ \$0 tax

### **Paying Yourself**

- Grant income can be used for personnel costs, including paying yourself as a sole proprietor.
- > Your net profit is the equivalent to your salary or wages.
- Net profit can be found on line 31 of your Schedule C.
- Grant income can be used to increase your net profit.
- Money that you pay to yourself is not deductible on your tax return.



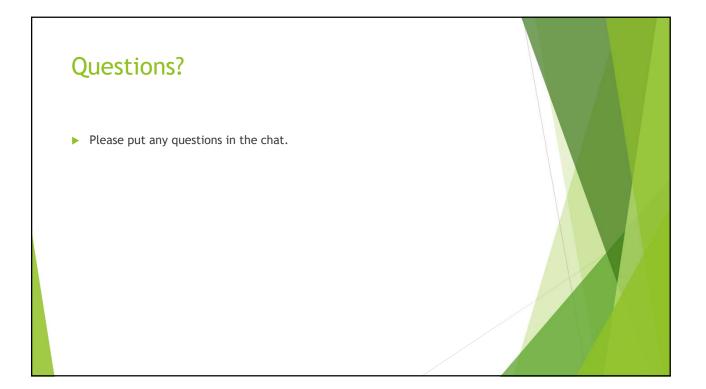
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### How to lower your taxes

Good recordkeeping is the best way to lower your taxes!

- Keep track of all business income and expenses.
- Record your child care hours including hours spent doing child care work when children are not present.
- Categorize your expenses correctly to get the most tax benefit possible.
- > Don't forget small expenses like business miles and extra meals.
- Don't wait until the end of the year to do your bookkeeping.
- Attend a webinar on tax preparation for child care providers or read any of Tom Copeland's materials on this topic.
- Hire a tax preparer who understands the child care business and prepares tax returns for other child care providers. Ask lots of questions.



### **Thank you!**

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