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CIVITAS STRATEGIES

Opportunities Exchange

Taxes, Incorporation, and Other Compensation Strategies for Home-Based Providers and Small Centers

Presented by:
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Change NOW!

Introductions & A Little About Us

Gary Romano, Civitas Strategies

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Disclaimer

Today's Discussion

Why taxes? → Opportunities → Change at Scale

Why Taxes?

Voices from the Field

Kelly Matthews, Wisconsin Early Childhood Association

Melinda Weber, United Way of Massachusetts Bay

- Key challenges observed:
  - Informational
  - Technical
  - Monetary
  - Familial
- Potential and lost opportunities

Why Do Taxes Matter to Small Business Owners?

Pay an average of 19.8% of their revenue in taxes (US Small Business Administration)

Accordingly, many small business owners treat tax mitigation as part of their compensation

However, most child care providers lack access to:

- Solid record keeping systems
- Any tax advice and planning
- Even mediocre tax preparation

The Opportunity For Gain

- Based on a sample of real child care business taxes:
  - Average increase of over $7,603 in earnings
  - Average four red flags for audits
- This translates to a 12% increase in revenue.

A 12% increase based on this average will be $176,575 in 25 years.

Typical Family Care Provider Taxation: Rates

- Child care businesses are usually sole proprietorships or single-member LLCs (both are taxed in the same way)
- Sole proprietorships pay:

  Self-employment tax of 15.3% on 92.35% of their profit

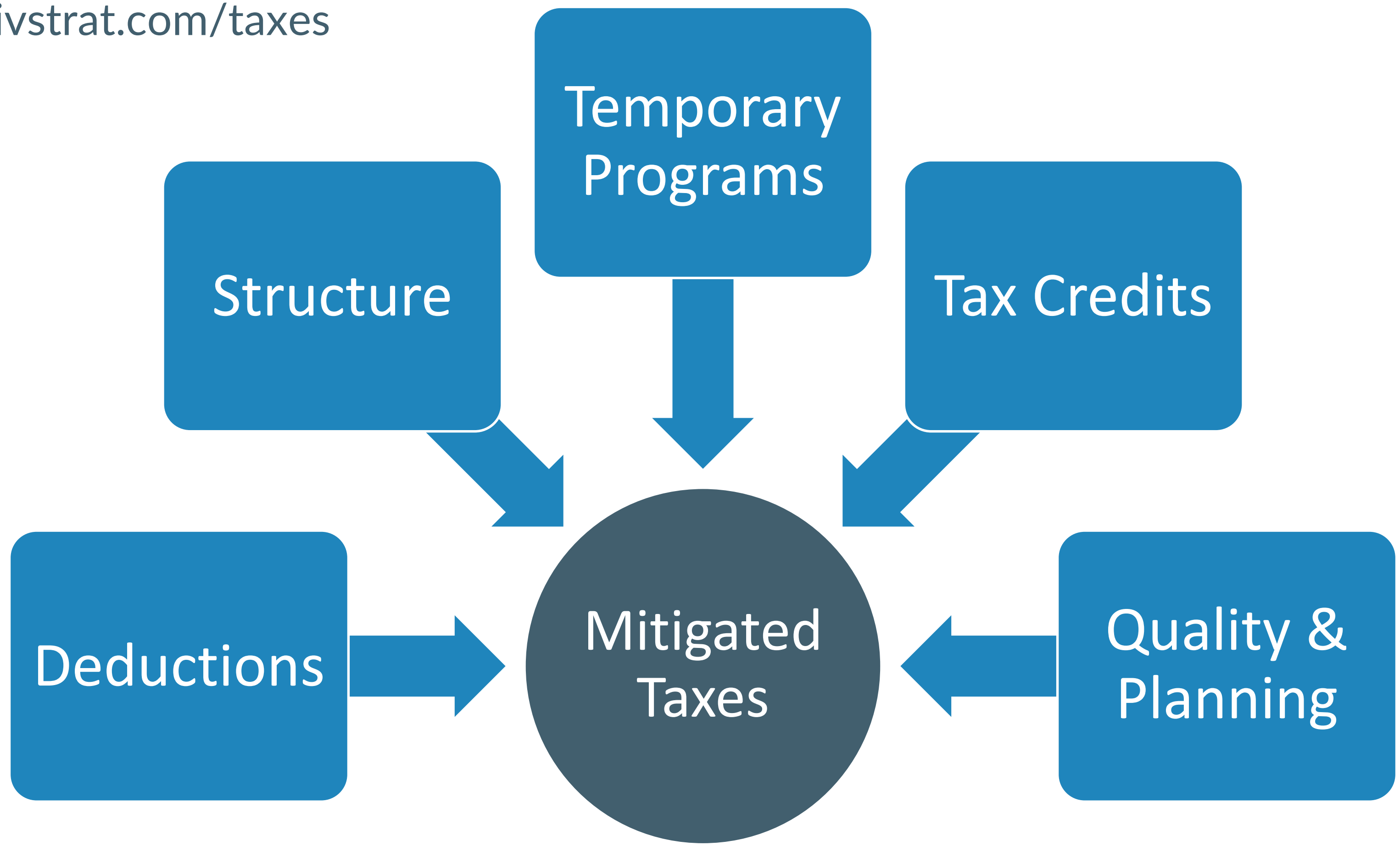
  Their marginal income tax rate less 20% Qualified Business Income Deduction
- S corporations or LLCs taxed as S corporations

  Face similar rates due to poor tax preparation

Opportunities

Opportunities for Tax Impact

Free tax resources available at
https://www.civstrat.com/taxes



Opportunity 1: Deductions

- All the typical business deductions
- Unique rules for business use of the home
  - Exclusive use
  - Regular use
  - Includes common areas
  - Disproportionately beneficial
- CACFP Standard Tier I Rates
  - Every case seen – higher than costs

Result: opportunities for disproportionate deductions

Opportunity 2: Structure

- Dominated by sole proprietorships
- S Corporations or LLCs as S Corporations growing especially among family child care
  - Liability protection
  - Tax savings opportunity is often not realized
- Partnerships rare

Compensation and Structure: S Corporations

Advantages

- Reasonable compensation vs Profit (big one!)
- Liability Protection
- Both Salary and Profit count for loans

Disadvantages

- Higher costs of prep and fees
- Self preparation is more difficult

Opportunity 3: Temporary Programs

Employee Retention Tax Credit	Families First Coronavirus Response Act Leave
• Revenue, government order, startup • $255,000 on average	• Covid, quarantine, home school/care • $2,500 on average

Claims for 2020 close in April 2024

Claims for 2021 remain until April 2025

Free information on these programs at https://www.civstrat.com/funding-resources

Opportunity 4: Tax Credits

Tax credits are more beneficial than deductions

Luz – effective tax rate of 31.8%

Let’s say she gets a $1,000 deduction and a tax credit

Deduction: $1,000 x 31.8 = $318.00 in taxes saved

Tax Credit: $1,000 = $1,000 in taxes saved

Key Credits

The Small Business Health Care Tax Credit: Healthcare premium support

Employer Credit for Paid Family and Medical Leave: Credits for family and medical leave

The Employer-Provided Child Care Facilities and Services Credit: Aids businesses providing employee care benefit (including contracts)

Setting Every Community Up for Retirement Enhancement (SECURE) Act: Supports new and ongoing retirement plans

The Work Opportunity Tax Credit: Funds for hiring within certain groups

Opportunity 5: Quality of Returns

Preparation relies heavily on the provider

Preparation industry is a “puppy mill” driven by volume and Earned Income Tax Credit Program

Have not seen a return without an error in two years

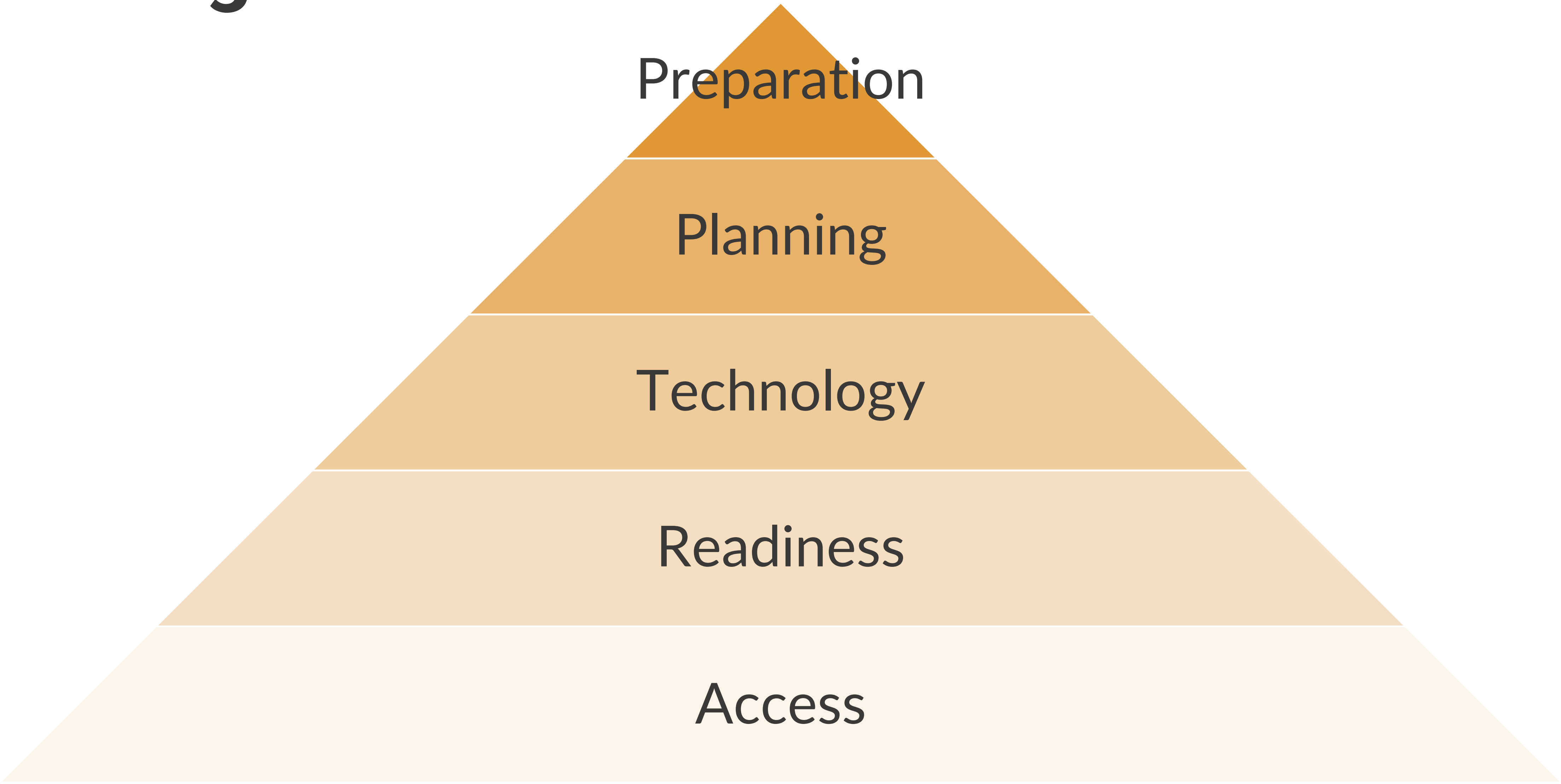
No Advisement

Typically paying $500-$1,500 for preparation

Provider must rely on their own knowledge and data (The era of the shoebox with receipts is over)

Change at Scale

Change At Scale



Access: Pandemic Tax Credits

There is still time for every provider who is eligible to get the ERTC or FFCRA Leave

Challenges include spreading the word and avoiding high fees (15-25% of the total credit)

Early Learning New Hampshire – Line coaches are sharing information, determining eligibility, and supporting pursuit

Readiness: For Tax Season

Organization and knowledge is a key challenge

Need to understand what they are taxed on and why

Prompts on what is deductible

Easy ways to communicate information to preparer

Home Grown Tax Preparation Workbook

Technology: to Leverage Investments

Organization is a key issue – CCMS can have an impact

Simple Apps – take providers though complex choices

Self-preparation – easy, scalable, and less likely to be audited

WECA Self-Preparation Guides - Step by Step process for applying using TurboTax, Tax Cut and HR Block, Includes the instructions for family care

Planning: All Year Long

- Tax and financial planning are key
- Well-resourced business owners have reviews before the end of the tax year
- Knowing about options and credits
- Also step by step support in decisions
- Coaches can do many if not all the strategies
- Opportunities Exchange/Civitas Strategies Retirement Issue Brief

Preparation: The Holy Grail

The "train a CPA" model has not sustained

The person leaves and then ends

Not the business model

Option 1: Internal Tax Preparation

Training takes time and investment

Single point dependent

Option 2: Centralized Approach

Nonprofit of B Corp focused on FCC taxes

Leverages technology and staff

Questions?

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Thank you!

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