

TAX CONSEQUENCES OF GRANT FUNDS FOR HBCC PROVIDERS

The general rule is that all income received is taxable. The only exception would be if the source of the funding specifically states that it is exempt from either federal or state income tax purposes.

In general, you must recognize taxable ordinary income regardless of how you choose to do business (corporation, LLC, partnerships, sole proprietors, etc.). Speak with a tax advisor to understand the precise implications of how a grant will be recognized and filed as part of your tax statement, generally for the year in which the grant was received. Also, consider how purchases made with the grant might be deductible.

Given the recent circumstances related to the pandemic, it would be prudent to seek professional advice on this matter regardless, in the event that any revisions have been made to current regulations.

Prior to Grant Award: It is advised that Intermediaries inform applicants of the above potential tax implications at the very least, prior to signing a grant agreement and receiving grant funds.

Post Grant Award: The Intermediary should review appropriate follow-up documentation with legal, financial or tax counsel related to the form document(s) it should issue to the Internal Revenue Service and Borrower by January 31 of the next year which identifies the amount of the grant that was awarded during the tax year the grant was awarded. This could be done by a 1099-MISC Form (Miscellaneous Income) or other documents as deemed appropriate.

Advice to Providers (excerpted from: What are the Tax Benefits of Receiving a Grant? By Tom Copeland).

Family child care providers must report as income the amount of a grant they receive as income. This includes materials purchased by the funder and given to the provider.

The value of the grants received under this program may be deducted on a provider's tax return following the regular rules of business deductions. In most cases there will be little, if any, impact on a provider's tax return.

If providers receive materials through a grant they should save records showing the value of the materials they received. If the shipping invoice does not show the value of the materials, they should ask for a copy of an invoice from the funder.

If providers pay for expenses directly (trainings, etc.) they should make a copy of the receipt for these items before sending the original receipt to the funder.

Examples:

I. A provider receives a \$250 grant and buys \$250 worth of children's materials. She uses these children's materials only during child care hours. She would report:

Income: \$250

Expense: \$250

No tax owed.

II. A provider receives a \$250 grant and is sent \$250 worth of children's materials. Her own children use these materials after day care hours and her Time-Space Percentage is 35%. She would report:

Income \$250

Expense: $\$250 \times 35\% = \87.50

$\$250 \text{ income} - \$87.50 \text{ business expense} = \$162.50 \text{ taxable income}$

Is it worthwhile to receive a grant?

Yes!

Some family child care providers are reluctant to apply for a grant when they realize they must report any grant they receive as taxable income.

But, they forget that they can deduct items purchased with the grant money as a business deduction. In many cases they can deduct 100% of the grant and will therefore pay no more in taxes. If you do owe a little more in taxes after receiving a grant, the amount is usually very small.

In the second example above the provider will owe taxes on \$162.50. That means paying between about \$49 and \$65 more in taxes (Social Security/Medicare/Federal and State income taxes). That's a small price to pay for getting a grant worth \$250!

Additional resources:

<http://tomcopelandblog.com/tax-preparerinsurance-directory>

<http://tomcopelandblog.com/irs-tax-formstax-changes>