

EDUCATORS AND DAY CARE PROVIDERS



**Tax strategies for teachers,
day care providers and
education professionals**



EDUCATORS

This provides an overview of the deductions that may be allowable to educators and those studying to become educators. While in most cases the IRS treats educators like other taxpayers, there are some distinct tax benefits extended to those in teaching.

Income

Income in the form of salary and wages to educators who are employed by any public or private educational institution, medical teaching facility or community school district is generally taxable and subject to Social Security and Medicare tax.

Other common non-salary earned income and compensation may be classified as self-employed income. This income is not only subject to income tax, but also may be subject to a 15.3% self-employment tax. Withholdings are rarely taken out of this self-employed income and quarterly estimated taxes should be paid for federal, state and self employment tax obligations.

Examples of typical self-employed educator income are:

- Substitute teaching income when employed as an independent contractor
- Payments for research studies
- Payments for clinical studies
- Speaker fees
- Author royalties and fees for published materials
- Consulting fees
- Endorsement and sponsorship fees

Excludable Income

Some forms of compensation to educators may be excluded from income. They include:

- Meals, when it is for the convenience of the employer
- Lodging, if on campus and if accepting the lodging is a requirement of the job
- Faculty Housing on an educational or medical research campus, if adequate rent is charged and/or valued as compensation
- Scholarship and Fellowship Grants to candidates for a degree at a qualified institution
- Tuition Reductions extended to educational employees

- Athletic Scholarship Grants to candidates for a degree and participation in athletics

Caution: Payments to individuals who teach or conduct research as part of their degree curriculum are not excludable from gross income and may be taxed.

Tip: Tax laws are liberalized regarding employer-provided meals. If provided for the convenience of the employer, they are not only excludable from income for teachers, but 100% (formerly only 50%) deductible for the educational institution.

Expenses

Deductible Expenses

A common mistake made by teachers is not keeping track of out-of-pocket expenses, including mileage deductions. How often have you purchased supplies for your classroom which were not reimbursed? Some of the most common deductible expenses include:

- Union dues, fees, benefit assessments
- Copies
- Computer supplies for the classroom
- Books for the classroom
- Research materials
- Supplies; pens, pencils, markers (for class)
- Teaching aids; pointers, transparencies, models, etc.
- Software
- Education expenses for maintaining or improving required skills
- Convention attendance expenses
- Education expenses to meet the minimum requirements of a job
- Certain education expenses to meet the requirements of a new job
- The cost and upkeep of a uniform including cleaning, if required for the job and not common attire
- All job hunting expenses, if in the same trade or business
- Unreimbursed expenses for:
 - tuition, books, lab. fees
 - professional society dues
 - professional journals fees

Also remember mileage, meals, and travel expenses. Mileage can be deducted whenever you go to or from your place of work from a non-home location or to another job.

Unfortunately, these expenses for salaried teachers are considered itemized deductions allowable only in excess of 2% of your income

when combined with other expenses, but if you are treated as a self-employed contractor you may deduct 100% of such costs as business expenses.

Tip: Through 2007 (and potentially 2008 pending legislative action) up to \$250 spent for out-of-pocket purchases of classroom materials may be deducted without itemizing. To qualify you must be a full-time K-12 educator. What can you do with excess expenses subject to a 2% of income threshold as a misc. itemized deduction? Donate! Collect your receipts, fill out a non-cash donation form and have your school acknowledge you donated the items to the school. If done properly, it reclassifies your expense as a charitable donation and avoids the 2% misc. deduction income threshold rule.

Tip: How can you tell whether you are considered an employee or self-employed? If you receive a W-2 they consider you an employee. If you receive a 1099 you are being viewed as a contractor (self-employed).

Non-deductible Expenses

- Commuting expenses (from home to school and back)
- Travel as education expenses
- Job hunting expenses, if it is for a first job
- Job hunting travel expenses, if personal activities predominate
- Job hunting expenses in a new career field
- Foreign convention attendance, unless directly related to current job performance and “reasonable in location”

Tip: Technical manuals and books with permanent value are considered capital expenditures that must be depreciated over their useful life, not fully deductible in the year purchased.

Home Office

Rules may enable a deduction for use of your home as an office if the area in your home is:

- Used exclusively for your career trade or business
- Used consistently
- If not in your home, then a separate structure from your home on your home's premises
- Your place of business to conduct meetings with business associates, customers and/or clients

- Used for the convenience of your employer
- Used as the sole place for you to conduct the administrative duties of your trade or business

This break is especially good for those who teach out of their home, such as tutors and music teachers.

Caution: The rules for business use of your home can be very complex and are highly scrutinized by the IRS. It's wise to seek advice on your particular situation.



DAY CARE PROVIDERS

As a subset of educators, day care providers warrant discussion regarding income, deduction of business expenses and the business use of your home.

First, you need to consider how you are viewed in the eyes of the IRS for your day care activity.

- **Independent day care provider.** You offer day care out of your home or a separate location. The IRS treats you as a “self-employed” worker.
- **Employee.** You work for a day care center, they pay your wages and withhold taxes. You receive a W-2 at the end of the year. The IRS treats you as an employee, just like other wage earners.
- **Contract labor.** Perhaps a day care center hires you on a spot basis and pays you a lump sum. At the end of the year you would receive a 1099. In this case you are considered “self-employed” by the IRS.

It is important to know how you are viewed in the eyes of the IRS to take full advantage of your tax situation.

Income

If you are an independent day care provider or contract labor, your income is typically self employed income and must be reported on a schedule C with your 1040 return. Your customers (parents) do not withhold any social security, federal or state taxes, so you are responsible to pay quarterly estimated taxes for your state, federal and self-employment tax (15.3%) obligations. Conversely if you are an “employee”, half of the self-employment tax is paid by the day care. Your share (7.65%) is withheld from your pay for social security and medicare.

Allowable Deductions

You may deduct your day care business related expenses and your use of your personal residence to provide day care services to children, elderly or handicapped if:

- You are a qualified, licensed or state certified provider
- You complete and file Form 8829
- The day care service is provided on a regular and consistent basis as your trade or business

Tip: It is recommended that a separate checking account be used to keep your day care expenses separate from other expenses.

A check list of the most common expenses includes:

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| ■ Supplies | ■ Clubs |
| ■ Food and snacks | ■ Furnishings |
| ■ Advertising costs | ■ Telephone |
| ■ Cleaning and maintenance | ■ Baby supplies |
| ■ Laundry | ■ Postage |
| ■ Equipment | ■ Payroll |
| ■ Insurance | ■ Fees for daytime activities |
| ■ Business Mileage | ■ Education expenses to meet state certification requirements eg. CPR and First Aid |
| ■ Play toys | |

Home Based Day Care Deductions

Common day care business-use-of-home deductions are calculated on the percentage of your home that is used for the day care services and include that portion of:

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| ■ Property taxes | ■ Maintenance |
| ■ Mortgage interest | ■ Utilities |
| ■ Home owners insurance | |

Note: Family (home-based) day care providers can use standard meal and snack rates versus actual costs in deducting meal and snack expenses for eligible children.

Business use of home expense calculations can be tricky. Call with questions particular to your situation.

This publication provides only summary information regarding the subject matter. Please call with any questions on how this information may impact your situation.