Opportunities Exchange

Family Child Care Provider Financial Management Tool Kit

Opportunities Exchange developed the Family Child Care Provider Financial Management Toolkit to address the persistent challenge of low pay and long hours in family child care settings, which in part, has contributed to decades long declines in the supply of home-based settings.

While many initiatives offer "business training" to providers, this toolkit is designed to support individualized coaching that moves business training from theory to practice. The Toolkit is comprised of three interrelated documents:

Part 1 – FCC Financial Management Self-Assessment Tool *(see website)*

This tool is designed to collect data in key areas of financial management:

- Iron Triangle
- Compensation
- Risk Management
- Business Structure
- Tax Liability
- Debt & Liquidity
- Fiscal Management

Providers complete the self-assessment (with support from the coach if needed), and the coaching entity uses the information to prioritize and structure coaching. The tool should be adapted for the local context, (e.g., if providers are participating in an automation project, then some data will be available to the coaching team electronically and practices will utilize automation tools). Coaches can have providers complete the assessment again after the coaching engagement has ended and compare the baseline and post-intervention data to document coaching outcomes.

Part 2 – FCC Financial Management Coaching Guide

This guide offers background information on the key elements of early childhood education financial management. Each section focuses on one key element, offering explanations and context.

Part 3 – FCC Financial Management Coaching Companion *(see website)*

This document provides hands-on templates, links, resources and checklists for coaches to use in supporting financial management best practices. The Companion is meant to augment the toolkit with specific regional/local information to best tailor coaching to the local landscape.

FCC Financial Management Coaching Guide

The Context & The Challenge

There are multiple factors that impact the context in which ECE programs operate, among them -- federal, state and local ECE policy, regulations, program funding, cost of living, unemployment rates, minimum wage, and community economic development. To manage a business effectively, providers need a thorough understanding of the environment in which they operate so they can remain relevant and financially viable.

The context for ECE creates several challenges. First and most importantly, child care in the United States is treated as a *market-based service*. This means that the **price** of child care does not correlate well with the actual **cost** of delivering the service. The price of child care most closely correlates with the incomes of families in the community – so that child care prices are higher in more affluent areas, and lower in low-income areas. Therefore, when public reimbursement is based on the price – vs. cost – it hurts under-resourced lower-income neighborhoods (most often urban and rural communities).

This system also often hurts providers who serve infants and toddlers, because a smaller number of very young children can be served, it limits the income a provider can earn, and most parents are unable to afford a higher rate based on lower group size.

Rate-setting is even more complicated for home-based child care providers – where total revenue determines compensation, fixed costs can vary widely, and sometimes the cost of an assistant caregiver must be included. Moreover, home-based child care programs that seek to participate in publicly funded early care and education programs – such as child care subsidy, Head Start/Early Head Start, or PreK – must often comply with additional, more costly standards, and yet the public reimbursement rates are often significantly lower than their center-based peers.

Due to multiple reporting requirements (based on funding streams) effective and efficient recordkeeping is crucial – and becomes an integral part of the financial management process. Providers, already burdened with exceptionally long days to accommodate working parents, sometimes forgo new funding opportunities because of the arduous administrative burden they impose.

SECTION 1: IRON TRIANGLE

The Iron Triangle is a management concept specific to ECE that when applied to family child care promotes full enrollment, full fee collection and pricing for services that supports a sustainable wage for the owner/provider. Just as a triangle is stable, strong and balanced, so too can any ECE business be if all three "sides" of the triangle are managed with rigor. In order to manage a business using the Iron Triangle concept, providers need accurate and timely data regarding enrollment capacity and actual enrollment and revenue invoiced and collected.

In Section 1, this guide will cover full enrollment and full fee collection. Section 2, Compensation, will explore setting rates and the impact of rate setting on provider earnings.

Full Enrollment

Full enrollment is the key to earning income. While some costs are variable and will be less during periods of low enrollment (for instance, with fewer children enrolled, fewer arts and crafts materials are used), fixed costs (such as mortgage and utilities) must continue to be paid regardless of the number of children enrolled.

There are three key areas to support full enrollment – *marketing, customer service, and data management*. In order to successfully market their programs, providers need to understand their unique niche in the ECE landscape. They must feel comfortable that the tuition and fees they charge are reasonable, based on the local market, and they must understand how their program fits within that marketplace. They must also feel comfortable that the hours, days of operation and schedules (part day/part week) that they offer are competitive and responsive to parent needs.

Marketing

Once clear about the value, unique strengths, and market fit of their program, providers need to have multiple strategies in place to help parents find them – via website, social media, word of mouth, internet searches, and key community partners.

Many providers believe that "word of mouth" is the best means of marketing available to them. Families turn to trusted friends, colleagues, neighbors and family members when selecting an ECE provider. However, a growing number of millennials are turning to the internet as their first source of information. Thus, while informal practices are important, all providers should have at least a simple website that lists basic program information, some pictures that convey

the setting, prices, hours, ages of children served and contact information. Websites that enable electronic submission of enrollment forms and other required documentation, tour scheduling – and perhaps even virtual tours – can be even more helpful to families. Providers may also want to have a Facebook page to advertise their program; however, if the Facebook page is public (vs. only open to enrolled families), care should be taken regarding policies for posting pictures of children.

Some providers offer financial incentives (cash, gift cards, reduced tuition, etc.) to families that refer other families who enroll in the program. Testimonials from current and previous families should be included on all forms of provider marketing materials, websites, brochures, etc.

Providers can target their marketing by reflecting on their own experience. They can collect enrollment data regularly and review the data over time to identify trends that emerge. For instance, does enrollment dip at specific times of the year? Consideration of enrollment patterns and challenges can help providers to identify the tools needed to meet specific family recruitment needs and adjust their business accordingly.

Customer Service

Before a child is enrolled in a program, families looking for care must: hear about the program, contact the provider, take a tour, and complete paperwork. There are multiple junctures where a family might become frustrated or discouraged if the provider does not respond quickly, fully, and professionally.

A high level of customer service includes providing clear and accurate information on the website and on all social media, responding to inquiries in a timely manner, and offering multiple means by which a family can tour and enroll in the program.

Keeping a waiting list and staying in communication with families on the list is another way to help minimize the time it takes to fill a vacant seat. Since this is a time-intensive task, selecting a child care management software system with the capacity to automate and support wait list management, can provide a highly valuable resource.

Data Management

The third strategy critical for full enrollment is data management. Providers have to analyze current enrollment data to understand vacancies and to target their marketing efforts – for instance, they might have vacancies only for children of specific ages or with specific schedules. Providers need to proactively analyze data to look at kindergarten enrollment dates and the impact that those dates

will have on their future enrollment. Providers also need to review their waiting list regularly and maintain contact with those individuals – a task made much more manageable by software with a wait list management feature.

Given that families sometimes fail to give providers adequate notice of their departure from the program and that not all families on a waiting list will be available to begin immediately upon notification of an opening, full enrollment is an unrealistic goal. However, establishing an enrollment goal of 85% or higher and tracking actual enrollment in order to monitor trends will help meet this goal.

Additionally, providers should have firm guidelines about: 1) the advance notice needed prior to withdrawing a child from the program, and 2) the providers right to keep a portion of the advance payment/deposit that families made upon enrollment if they do not provide adequate notice. Because the percentage of families withdrawing from care is higher during summer months, the advance notice requirement can be longer than during the academic school year. This allows providers to better plan enrollment and intake schedules. It also encourages families to communicate any planned changes in advance.

Keeping slots full is a big job – and many home-based child care providers spend so many hours working with children that finding time for marketing and enrollment management can be a challenge. This is a key role that Shared Service 'Hubs' such as Staffed Family Child Care Networks can play – creating strategies and systems to collectively support marketing and enrollment so that providers have a steady stream of families waiting to enroll at any given point in time.

Full Fee Collection

Once children are enrolled in a program, providers must actually collect all of the revenue earned. This can be challenging, especially given the personal relationship child care programs have with parents. Additionally, some families may receive funding from multiple public and private sources that require the provider to track attendance and submit separate invoices based on the funding source. Critical to this task is tracking attendance information, generating timely and accurate invoices, tracking payments received, and implementing internal policies and funder requirements when payments are late or missed. A child care management software system can automate most of these tasks.

In order to improve collection practices, it isn't enough for providers to know that they "took in less revenue this month than last". Providers need to know how much was invoiced to each revenue source (parents, subsidy, etc.) and

how much was collected from each of these sources. Once an area of discrepancy is identified, providers can begin a more detailed level of investigation.

In order to effectively collect parent fees, providers need a set of clearly written fee collection policies and they need to implement these policies consistently. Policies should cover critical areas such as when parent payments are due, how they may be paid, and when late fees are assessed. While providers want to be flexible in offering parents multiple methods of payment, flexibility can increase challenges.

Providers should be highly discouraged from accepting cash as payment for services. Tracking cash is always tricky – it is easy to forget to create a receipt each time you take cash, but without a written receipt you have no proof of payment. Cash should be deposited into the business account in order to account for revenue, but it takes time to prepare deposits and travel to the bank. Finally, cash is subject to being lost, stolen, or spent on immediate needs – making it difficult to have a full accounting of business income.

Electronic payment systems are much easier to track, and much more likely to ensure prompt payment. However, credit card fees can be a challenge. Providers need to understand when fees are charged, and how much, and explore the feasibility of a policy that passes these fees on to the parents. A much better option for electronic payment is ACH transfers or low/no fee payment platforms (Venmo, PayPal, etc.).

Full fee collection and bad debt are two sides of the same coin. Bad debt is the percentage of parent fees not collected and number of unpaid days from state/local subsidy agency (reasons include: absences, lack of subsidy authorization, and failure to record attendance). Bad debt is an open receivable (or an asset) for the business on the balance sheet that would, with proper fee collection policies and procedures, instead be money (revenue) in the provider bank account!

The use of a child care management system (discussed below) for parent invoicing and automated payments should greatly reduce bad debt from parents. However, providers need to ensure that their fee schedule and their parent fee/enrollment agreement are clear, consistent, and updated. Providers must also follow all of the policies – such as late pick-up fees, late payment fees – outlined in the agreement consistently for all parents.

Providers may have multiple revenue sources that need to be invoiced and from which payment must be tracked and reconciled. These might include child care subsidy, PreK, Head Start/Early Head Start, or a military or employer

contract. Based on the contractual terms, providers will need to submit invoices and enrollment/attendance data to these funders and will need to record expected payments, track actual payments, note any differentials, and potentially re-bill as necessary.

Finally, providers need to have clear policies around writing off bad debt based on the aging of the receivables. Debts that remain uncollected after a fixed period of time are considered uncollectible and no longer appear as an asset (receivable) for the business. The policy for writing off bad debt needs to be consistently implemented annually.

Child Care Management Software

It has been noted that child care management software (CCMS) can be used to help providers fully implement best business practices. There are several off-the-shelf systems (including Procare online, Wonderschool, Alliance CORE from Early Learning Ventures, Brightwheel, etc.) that can be used effectively by individual providers or in the context of a Staffed Family Child Care Network to enable the provision of back-office services. See CCMS: Frequently Asked Questions

Many of the newer CCMS are "mobile first" – meaning that they can be effectively operated from a mobile device such as a smart phone or tablet. and are designed to be extremely easy to use. Providers who may not be comfortable using a desktop computer for financial or administrative tasks but who can successfully interact with Facebook, send text messages, or purchase goods online, may find that – with these new web-based products – they can successfully navigate an online CCMS.

It is difficult to overstate the benefits of moving from paper to software for managing a child care business. Providers are able to market their programs, enroll families, track/report attendance, maintain records for business and regulatory compliance, invoice/collect tuition, and communicate with families in a fraction of the time it takes to do these tasks manually. Added to this, the benefit of electronic tuition collection virtually always results in faster, fuller payment to providers.

If at all possible, the FCC coach should explore opportunities to assist providers in selecting and onboarding to a CCMS as a first and critical step toward best business practices.

SECTION 2: COMPENSATION

The amount a Family Child Care provider earns is based on the net income (all revenue less expenses) of their business and related benefits. The broadest view of compensation also considers the number of hours per week that the provider works (in other words if you earn $30K and currently work 70 hours a week, reducing your work week to 50 hours means your hourly wage went up by over $3 per hour!)

Tuition Rates

The primary source of income for most child care programs is the tuition and fees paid by families. Even programs that serve low-income children whose care is paid for by a government subsidy often find that the amount they receive is based on the local market price (that is, the amount most providers charge.) Figuring out how to establish rates (prices) that cover your costs, and fully collecting all fees owed, can be challenging.

Rates are established by each child care provider, and may vary based on the provider's professional credentials, experience, and program features. However, the single largest determinant of tuition rates is the income levels of the families served. Providers who operate in communities of moderate to high wealth will be able to charge much higher rates for their service. This is the primary reason why government subsidy should not be based on market prices. In most cases, providers serving families in low-income communities need to supplement revenue with additional funding sources.

Tuition rates and any fees (e.g., application, field trips, late pick-up, late payment, diapers) should be reviewed regularly by the provider in the context of rates and fees charged by other comparable programs and actual costs. Tuition rates should be raised as necessary and possible within the perceived limitation of what parents can afford.

Setting part-time rates

Full enrollment is made more challenging by part-time schedules, which require specific matching of children in order for providers to remain "whole" or "full". To address this complexity, providers should take care in calculating the part week rate. Providers need to take the daily rate for full time and multiply that by approximately 20% to 40% (depending on the number of days in care) to get a part time daily rate. The fewer days in care, the higher the add-on percentage and resulting daily rate.

For example, if the daily rate for infants is $46.86, multiply that by 20% to get a part time daily rate of $56.23 for parents seeking three days of infant care. For two days, multiply it by approximately 40% to calculate $65.50. This ensures that a provider can fill one slot with two children without losing money.

Because a provider should never lose money by doing part week rates, the general rule should be that part week fees should be at such a rate that if a provider enrolls two children for two days only, the provider earns more than the full-time rate for one child. Because the provider is actually working with two children and two families and two sets of paperwork, this strategy recognizes the increased costs to handle the paperwork, family engagement, and other supports and services required for the two children using the single spot.

Government/Public Funding

There are multiple sources of federal, state, and local funding for ECE services and providers can maximize their compensation by increasing the number of funding streams for which they qualify and enroll. In some cases, these dollars are awarded directly from a government entity; in other cases, they flow through an intermediary organization under contract with government. Laws and regulations set the amount of public funding and the purposes for which it can be used. While laws are written and voted on by elected officials, appointed and non-appointed government employees usually establish regulations and administrative systems that control and may restrict the use of public funds. In addition, intermediaries may have latitude regarding the administration of funds. Both non-profit and for-profit childcare organizations can receive most types of public funding.

Available public funds will vary based on the state or municipality in which the child care program is located as well as the children and families served but typically include:

- Small Business Administration grants and loans
- Child care subsidy payments
- Head Start/Early Head Start contracts
- Public PreK funding
- Child Care subsidy to serve military families
- Stipends, grants, and higher reimbursement rates via Quality Rating Improvement System
- Child and Adult Care Food Program
- Wage subsidies from programs like TEACH or WAGES
- Federal Refundable tax credits (such as the Earned Income Tax Credit, the federal Health Care Premium Tax Credit)

- State or Local Government Tax Credits or Abatements (for PreK tuition, staff wages, facility improvement or other program expenses)

Private Sector Funding

While it represents a relatively small percentage of total child care funding, support from the private sector – foundations, employers, and individual donors – can also be worthy of exploration. In some communities, employers are willing to help subsidize the cost of care or create provider networks to help their employees find care. United Way is another helpful partner for child care programs seeking to tap funding from business or philanthropy.

Many, though not all, of these contributions are restricted to nonprofit entities, and therefore need to be disbursed through an intermediary – such as a provider network.

Employment Benefits

To ensure that FCC providers earn a livable wage, both income (revenue) and benefits must be considered. Three primary benefits can improve the physical, mental, and long-term health of providers and help these businesses be competitive with other employment options. These include: paid time off, health insurance, and a retirement plan.

Paid holidays – FCC providers typically close for nationally observed holidays throughout the year. While public funders generally allow providers to receive payment for up-to a maximum number of closed days per year, providers need to assert such policies for parents. Unless they do so, they may not actually receive paid holidays at all.

Paid Vacation time – Paid time for vacations and other personal needs can also be structured into the operation of a FCC business. One way to do this is to write into the parent contract that fees are paid weekly, even when the program is closed for holidays/vacation as well as when families themselves are on vacation and do not need child care. Alternatively, the weekly rate can be increased to include the additional cost of days when fees are not collected – such as holidays and vacation.

Health Insurance – Most Americans receive health insurance, for themselves and their families, through their place of employment. Health insurance is extremely costly for a small business however, based on income, many providers can find affordable insurance plans on the government *Health Care Exchange*. Additionally, ECESharedResources has an affordable *Docs by Phone* plan that

covers any member of your family. This plan includes telehealth visits with a range of board-certified doctors for routine medical needs.

Retirement Plans – FCC providers should be encouraged to create retirement plans for themselves. As explained in Family Child Care Record-Keeping Guide by Tom Copeland (Ninth Edition, 2019) a qualified retirement plan is a savings and investment plan that meets IRS requirements for favorable tax treatment (e.g., pretax contributions, tax deferred gains). While FCC providers may find saving money each month a challenge, there are strong tax incentives for doing so. For most IRA options, the contribution reduces taxable income and defers taxes on interest earned. Each type of qualified plan has specific rules around annual allowable contributions and other matters.

SECTION 3: RISK MANAGEMENT

FCC providers face a great deal of risk related to the operation of their businesses. While compliance with all local, state and federal laws and with quality rating improvement and/or accreditation standards can lessen the exposure, providers will require insurance to protect them from unforeseen circumstances.

The first step in risk management is to fully meet all licensing requirements and any other local or state regulation. Providers should regularly conduct fire and disaster drills and ensure that they have policies in place to document that they have met this requirement.

Providers should understand the insurance policies that best meet their needs, how to ask the right questions in order to secure effective coverage, and how to select an insurance agent that understands the business of family child care. Insurance, like most industries, uses language and terms that are specific and can be difficult to grasp. Providers should not be intimidated or discouraged by this!

Insurance policies vary in price based on several factors including the amount of coverage offered. Ideally a provider needs a business liability policy that provides $1 million per occurrence (or for each incident) and $2 million aggregate (or the total amount that the policy will pay out in a single year).

In addition to shopping for insurance based on the amount of coverage, providers should understand if the attorney fees to defend a claim are deducted from the total possible payout, and look for policies that pay attorney fees separately. Finally, providers should be aware that the full cost of a business liability insurance policy is tax deductible.

Most homeowner's insurance policies cover only a small amount of household property damage or loss (usually up to $2,000). A provider needs to understand the details of coverage she already does (and does not) have through her current homeowner's policy. In addition, she needs to understand if her business liability insurance policy includes some business property coverage. If the current coverage (through one or both of the above-mentioned type of insurance policies) is inadequate, a provider can purchase business property insurance to adequately cover loss or damage to her home and/or its contents.

Providers also need business insurance (or commercial insurance) if they transport children in their own cars. Providers need to contact their current car insurance agent to get a written statement that the policy they already have will cover the provider, the children, and the vehicle if there is an accident. The agent can also add a statement to the certificate of insurance that the policy is a business or commercial policy. If the agent is unable or unwilling to provide either of these types of written documentation of insurance coverage, then the provider needs to either purchase additional coverage or stop transporting children in her car. Because the cost of business insurance is high, it may not be financially viable to transport children.

SECTION 4: BUSINESS STRUCTURE

FCC providers have several choices regarding how best to structure their business – self-employed sole proprietor, general partnership, limited liability company, or corporation. There is no one right or wrong way, but each choice has legal and tax implications, some of which may vary by state, so those establishing their businesses and considering a structure other than the self-employed sole proprietor should consult a lawyer and tax professional.

A good resource for understanding options is: Family Child Care Legal & Insurance Guide: How to Reduce the Risks of Running Your Business by Tom Copeland and Mari Millard, 2004.

All providers should apply for a federal taxpayer identification number (EIN) to avoid having to use a Social Security number on official documents and thereby minimize the risk of identity theft and fraud. There is no cost and it is a simple online process: Applying for an IRS Identification Number.

The EIN should be provided to parents who want to claim the child care tax credit and used on business tax forms (Schedule C and Form 1040SE). If a provider is opening a new bank account, signing a contract, or entering into another type of business transaction, she should use her EIN. The provider Social Security number is used on the IRS personal Form 1040.

SECTION 5: TAX LIABILITY

As sole proprietors/business owners, home-based child care providers are responsible for paying federal, state, and local taxes on their earnings. However, as a small business, FCC homes are also able to deduct a host of expenses that can significantly offset the amount of tax owed Careful tracking of these costs can have a significant, positive impact on annual provider earnings. However, accurate tax preparation can be complicated by the unique calculations applied to family child care business deductions.

All FCC providers should diligently track: 1) their expenses, 2) the time they spend working, 3) the number of meals and snacks they serve, and 4) the square footage in their home used by the business. Carefully tracking each of these measures will ensure that they are able to maximize the tax deductions available to them as family child care business owners. By maximizing tax deductions – ordinary and necessary business expenses – to the fullest extent of the law and thereby minimizing net profit, FCC providers significantly reduce their tax bill. This increases the amount of money that they earn **AND KEEP** each year.

FCC providers who structure their business as a sole proprietor, and earn a net profit of $400 or more on Schedule C, will need to pay self-employment tax (basically Social Security and Medicare) which is currently 15.3% of business profit. Self-employment taxes require filing of an additional schedule – Schedule SE Self-Employment Tax.

Unfortunately, most providers are not keeping adequate records, which results in paying more taxes than necessary. Technology tools, along with back office supports from a Network Hub, can make record keeping easier and the business more profitable. For example, a typical provider earning gross revenue of $46,000/year can reduce her likely tax burden from $5091 to $4019 – a savings of more than $1,000 – by carefully tracking expenses and hours worked.

Providers with young children may be able to demonstrate an adjusted gross income that qualifies them for the Earned Income Tax Credit (EITC), which not only lowers their taxable income but could potentially result in a refund even if they ow now taxes (because the EITC is a 'refundable' credit.) Additionally, single providers with an income of less than $49,000 and married providers with family income less than $85,000 are eligible for tax credits that lower the cost of health insurance purchased on the government health care exchange. In some income brackets the health insurance can be completely free.

Time-Space Percentage

Tax law changes year-to-year in specific areas, and coaches are not expected to be knowledgeable about the IRS tax code or skilled in tax preparation. Rather, coaches can support providers in tracking expenses by category (home repair, utilities, office supplies, food, etc.) and in tracking data for use in calculating the time-space percentage so that the appropriate deductions can be made.

Expenses should be organized by category because the IRS regulation stipulates which categories can be deducted in full and which can only be deducted in part. The full value of business expenses that are EXCLUSIVELY used for the business can be deducted from gross income. Shared business expenses – those expenses that are shared between personal and business use - can be partially deducted. The basis for determining what percentage of those expenses can be deducted is called the time-space percentage, which is entered on IRS Form 8829 Expenses for Business Use of Your Home.

The first step in calculating the percentage is recording how much time a provider's home is used for operation of the business. This includes working hours when children are present – the first moment that a child walks through the door in the morning and the moment that the last child walks out the door in the evening - and working hours when children are not present – and the provider is cleaning, record keeping, preparing meals, and performing any other task related to her business.

The second step in calculating the percentage is recording the square footage in the home that is "regularly" used for the business. In determining "regular" use, consider the availability of the room during the business day and the frequency with which it is used. Rooms in the home that are typically listed as being regularly used include the kitchen, living room, dining room, bathrooms, hallways, storage rooms, bedrooms, and laundry room. The only square footage that is eligible to be counted is that which is part of the structure of a building. So, while a deck can be included, for instance, an outdoor play area cannot.

With these figures in hand the math is simple (this can be calculated from the Time-Space Percentage TAB in the Budget Template documents found on the OppEx website and in the *Coaching Companion*.

1. Divide the number of hours the home is used for business by the total hours in the year (8,760 hours).
2. Divide the number of square feet in the home used regularly for the business by the total number of square feet in the home.
3. Multiply the two numbers together to generate the time-space percentage for IRS Form 8829 and for use in determining how much a

provider can deduct for her shared person/business expenses from her gross revenue.

There are additional steps for a provider to take if one or more spaces in the home are used exclusively for the business. The time-space percentage for exclusive use is added to the time-space percentage for the rest of the home to create the time-space percentage for the entire home. FCC providers need to calculate the time-space percentage annually based on the tracking of hours and space conducted throughout the year.

Providers are not required to use the time-space percentage as the only way to determine what percentage of shared expenses can be deducted from their income. They might, for instance, use a combination of this method with actual use for a shared item of relatively large value, such as outdoor play equipment. The actual usage should be tracked for a minimum of two months during the year in order to document the actual percentage that a provider determines for a specific item.

Providers (or their tax preparers) need to understand the rules around the timing of deductions. In most cases the cost may be deducted in one tax year, but both the cost of the item and the type of item – depreciation – can trigger multi-year deduction requirements.

Finally, providers (or their tax preparers) need to understand the IRS rules around vehicle expenses, including mileage, and home expenses, including home improvements.

SECTION 6: DEBT & LIQUIDITY

Debt and liquidity are two sides of the same coin. Debt is money that a FCC provider owes. Liquidity is a provider's ability to access the cash that she needs to operate her business. The balance sheet is a financial report that includes both assets (segmented by liquidity) and liabilities – including debt -- and is considered an essential complement to the Income (profit and loss) statement for assessing financial health of a business.

Debt can take many forms, including: credit card debt, college loans, car loans, bank line of credit, mortgage, or other type of loan. Small businesses often need to access debt either at start-up or at challenging points in time during the life cycle of the business. Debt isn't necessarily bad, but some debt includes high rates of interest that can wipe out profitability and de-stabilize a business.

Liquidity is essential for the smooth operation of a business. If a provider suddenly needs to complete a major home repair in order to remain open, for

instance, she needs a means to pay for that unplanned expense. Cash or credit can be used, but providers need multiple means of paying for both the ongoing, typical expenses tied to operations and the unanticipated expenses that may arise.

There are many types of financial counseling available to individuals and businesses. Most of these are available free of charge to all or minimally to those with incomes at 150% of Federal poverty level or below. Services include: budget and credit counseling; financial health counseling; credit report counseling; debt management program; pre-purchase housing counseling; foreclosure prevention and mortgage default counseling; and, reverse mortgage counseling.

Different than a bank and a certified financial counselor, Community Development Financial Institutions (CDFIs) offer low interest loans based on community need. If a provider has a current loan of any kind, exploring alternative loan options via a CDFI could potentially save money on interest and fees – depending, of course, on the possibility that the current loan could be pre-paid.

FCC providers need coaching in two areas – in accessing reasonably inexpensive funds when times are bad (liquidity) and in assessing their ability to continue to carry their current level and type of debt. Coaches are not financial advisors but they can play an important role in helping providers to access this set of expertise.

Providers should be encouraged to reach out to their bank to learn about the various account types, their options, and costs. Issues such as monthly fees and interest rates should be discussed, along with the possibility of securing a bank line of credit. Providers should consider applying for a line of credit before they need it so that it will be an option for low-interest funds if needed. Providers should understand how to access the line and how charges will accrue based on use.

Providers should also be encouraged to use online banking and to link, if possible, data from their online banking system to their accounting system.

Providers should review all current debt to ensure they understand the interest rate and terms on all money that is owed. Once providers see the financial impact of the various types of credit that they carry, they may need help in negotiating different terms and payment plans.

SECTION 7: FISCAL MANAGEMENT

Budgets and financial statements are critical tools for providers to use in documenting, tracking, and managing the financial performance of their businesses. While many providers depend on the level of funds in their bank accounts as their primary financial report, budgets and financial statements are critical to providing a comprehensive picture of financial status.

Fiscal Reports

Financial reports allow providers to understand their current financial position, to better manage their business based on the current financial position, and to plan for their future by generating fiscal scenarios. Budgets and financial reports allow providers to know the answers to critical questions such as:

- How big is your business (the amount of your **current** annual operating budget)?
- Does your business earn more income than you incur in expenses?
- How much are you earning per year? Is this sufficient for you to continue to operate for as long as you choose?
- Are you collecting income at the rate that you had budgeted? (For instance, if you estimated that you would collect 98% of the parent tuition you invoiced but you only collected 95%, then you would answer "no" to this question.)
- Are you meeting your enrollment goals/projections?
- How does your current financial performance compare to previous years?
- How much cash do you have on hand?
- Of every dollar earned, how much is retained (vs. spent to operate the business)?

There are multiple types of budgets and they can be used for multiple purposes. A start-up budget includes one-time and ongoing costs, and typically includes a phased enrollment and staffing plan. Operational budgets typically are based on the previous year's actual performance, with updates based on changes in the context or business environment. All budgets should state the time period covered and should include revenues and expenses. Assumptions should be clearly stated so that those looking at the budget can easily understand how calculations were made.

The basic fiscal reports include:

- Profit and Loss statement showing income and expenses for the month and year-to-date and comparing actual to budgeted

- Accounts receivable and aging
- Cash flow projections
- Audited financial statements (these are issued by external auditor, with accompanying management letter and notes, and may be required for non-profit FCC providers and/or those with government contracts requiring this level of fiduciary oversight)

The *profit and loss statement*, allows providers to see their actual performance in comparison to what was budgeted. Depending on the format of the report, they can also see actual performance in comparison to the previous month, to the same month last year, or other timeframes. The income statement typically includes current month and year to date (YTD) data so that providers can see the larger context of operations. Timing issues that may impact one month's performance should be balanced out by YTD data.

Accounts receivable and aging reports provide a detailed accounting of all money owed to the provider, by source, and the amount of time it has been owed. The longer a debt goes without being paid, the less likely that the provider will be able to collect funds, so aging reports can help the provider keep unpaid bills from going too long and becoming uncollectable.

Cash flow projection helps providers see when funds will be more limited so they can plan and better manage expenses. In child care businesses, cash flow is typically tied to enrollment. When enrollment is low or inconsistent, so is cash flow.

Audited financial statements are generally only required when there is third party funding (such as PreK or Head Start) and the funder requires an additional level of fiscal oversight. In most cases, providers do not need an independent audit.

Accounting Software

Many ECE providers use either Excel spreadsheets or QuickBooks to manage their fiscal data. QuickBooks is an on-line system that allows data entry and sharing from any internet accessible location. Use of automation for fiscal functions minimizes data entry errors; allows accurate and detailed revenue and expense coding; and allows accurate, detailed, and timely fiscal reporting.

Chart of Accounts

Sound financial management begins with a budget and a chart of accounts that allows providers to correctly assign all income and expense to the

appropriate category. As noted in the Tax Liability section, tracking expenses by category is also a fundamental step to maximizing deductions.

Opportunities Exchange has created an FCC Chart of Accounts template that is associated with the categories used by the IRS for reporting expenses on the annual tax return. It is highly recommended that FCC use this format for creating budgets in order to efficiently capture all deductible expenses.

In order to track the financial status of their program, providers should enter all financial information in an accounting software system such as QuickBooks. Most CCMS systems have a way to transfer revenue received into an accounting software system, so that only expenses need to be entered manually.

Fiscal Roles & Responsibilities

There are many ways for providers to gain access to critical financial information needed to operate a sustainable business. Some providers will use a *bookkeeper or accountant* (which could be paid or volunteer such as a family member). In these situations, providers will typically save financial records (income and expenses) and share with the financial contractor, monthly, quarterly, or annually. Reports will be created and shared with the FCC and can be used to complete annual tax filings.

If a provider uses outside help for financial recordkeeping, it can be useful to review documents that the provider receives, ensure they understand the information, and support them in making any needed modifications to the process.

Some providers manage all financial records themselves – and the level of skill in financial management varies widely. Many providers are actively managing critical elements of their business to make it sustainable; but a significant percentage of providers are quite unaware of where they stand financially and what actions could mean the difference between profitability and insolvency. Providers who do not currently have financial systems in place will need concrete evidence that skilled business management can have an impact on their bottom line. However, with guidance focused on helping them understand their current operation and identify opportunities to improve revenue and profitability, it is possible to help them move – step by step – toward stronger businesses.

A third group of providers are affiliated with family child care networks, most of which offer support with educational practices, quality standards, and other programmatic functions. Because of the nature of their relationships with

providers, these entities have an opportunity to widen their scope of services to include business services in order to strengthen the financial viability of these providers.

Summary

Because Family Child Care is such a critical component of the early care and education system, it is necessary to have a vibrant, sustainable FCC sector. Ensuring that providers have the resources and support to earn a livable wage, work a manageable number of hours, and support the needs of young children has tremendous value to the field.

The coach is not an accountant, tax preparer or auditor. However, the coach can provide basic supports to the FCC provider in assuring that systems are in place to allow for the collection and reporting of key fiscal data and can help the provider understand how to analyze reports to support sustainability.