

2018 SMALL BUSINESS YEAR-END LETTER



2018 was a good year for business taxes.

On the balance, the Tax Cuts & Jobs Act (TC&JA) was favorable for business owners. Most importantly, there's a new deduction called the Qualified Business Income Deduction (QBID).

Who gets to take the deduction?

Profitable business owners (excluding C-corporations) with taxable income under \$315,000 (married) and \$157,500 (single) will get the deduction. If you make more than that it gets complicated, so let's focus on folks below these limits first.

How big is the deduction? Taxpayers below these income thresholds will generally get to deduct the lesser of; 1) 20% of Qualified Business Income (QBI), or 2) 20% of taxable income minus capital gains.

What is QBI? QBI is closely related to profits. If your business is profitable you likely will have QBI. There are some exceptions. For example, business owners with an extremely high mileage deduction might be profitable but not have QBI. Similarly, profitable landlords might not have QBI because of high depreciation deductions.

Example: Paul is a single consultant with \$75,000 in QBI and no capital gains. His taxable income (after deductions) is \$57,701. His deduction is 20% of \$57,701, or \$11,540. This saves him \$2,539 in tax.

In this example, Paul could have gotten a bigger deduction if his taxable income was higher. For example, he could have taken a side job or married a spouse with adequate wages to increase his taxable income, and thus get a larger QBID. However, Paul would not want his taxable income to get too high.

That's because the rules are less favorable if your taxable income is above \$157,500/\$315,000 (single/married).

Above these levels it matters what type of business it is. For example, service business (e.g. health, law, accounting, financial services, performers, consultants, athletes, plus others) see their deduction phase-out above those income thresholds. Those folks may want to contribute more to their retirement accounts (if possible), or buy expensive business equipment to reduce their taxable income and qualify for the QBID.

Business that are NOT services (e.g. manufacturing, retail, plus others) can have taxable income above these levels and still get the deduction. However, their deduction is limited by other factors such as total wages paid to employees and the value of certain business assets. In summary, the QBID rules are favorable but complex, so work with a professional to optimize your tax savings.

A Few of the new business tax rules are not favorable.

Deductions for certain types of client entertainment (e.g. sports tickets) were eliminated. Furthermore, the Domestic Production Deduction for businesses with employees that make products in the USA was eliminated.

The TC&JA also eliminated the deduction for hobby expenses. The IRS can consider your activity to be a hobby and **not a business** if you do not have a profit in 3 out of 5 years.

If a loss scenario applies to your business, **it is important to show that you are trying to make a profit.** The following strategies might be helpful.

- Keep a set of business books.
- Use a separate business bank account.
- Keep a log of activity.

- Use a separate business credit card.
- Advertise

Did you pay for self-employed health insurance?

A self-employed taxpayer can deduct 100% of the amount paid during 2018 for medical insurance for him/herself, spouse, and dependents as an adjustment to income. Deductible payments for health insurance also include Medicare premiums.

No deduction is allowed for any month that the taxpayer is eligible to participate in a subsidized health plan maintained by an employer of either the taxpayer or the taxpayer's spouse.

The deduction is limited to net income from self-employment.

Have employees?

- If you are planning to give your employees a holiday gift, make sure it is de minimis and not in cash, otherwise, it must be included in wages.
- The IRS wants your W2 filings by Jan 31st. The same deadline applies to 1099-misc filings for independent contractors.
- If you purchased health insurance for your employees, you might qualify for a 2018 tax credit.
- Small employers (less than 50 full-time equivalent employees) who do not offer a group health plan to any of their employees may offer a QSEHRA (Qualified Small Employee Health Reimbursement Arrangement) to their staff. Employees pick their own plan on the open market and employers set-aside up to \$5050 (single) or \$10,250 (family) as a pre-tax company funded benefit.

Beware of misclassifying employees as independent contractors. The IRS has a form for misclassified employees to report you and they are actively pursuing businesses that do not comply.



Do you use your vehicle for business?

Proper documentation of business miles can make quite a difference in your bottom line profit. The following rules apply to mileage expenses:

Business Mileage Guide Methods:

Business transportation expenses can be calculated for tax purposes in one of the following two ways. In both cases, a record must be kept of business miles, commuting miles, personal miles, and total miles.

Standard mileage rate: This method can be used if you do not use your car for hire or operate a fleet. The rate for 2018 is 54.5¢ for each business mile driven.

Actual expense method: This method must be used if you are unable to use the standard mileage rate. It is to your advantage to use this method if your vehicle is costly to run or is over 6000 pounds. Records of all vehicle expenses must be maintained and applied to the business mileage percentage. These expenses include gas, oil, lube, repairs, tires, batteries, insurance, supplies, washes and waxes. The business use percentage of lease payments or depreciation is also calculated.

Deductible Mileage:

You can use the following three scenarios to determine how many miles you can deduct. Keep in mind that **commuting is not deductible**.

If you have an office or regular place of business outside your home, you may not deduct commuting miles to and from work or to your first and from your last stop home, but you may deduct mileage to a temporary work place and mileage to and from different locations for work during the day.

If you have an office in your home that qualifies for a home office deduction (see

below for qualifications) all of your business-related mileage is deductible.

If you work out of your home, but do not qualify for the home office deduction, the distance between home and your first stop and the distance between your last stop and home are nondeductible commuting miles. You should plan to have your first and last stops close to home to maximize the mileage deduction. A trip to the bank, post office or a nearby supplier can help increase deductible business miles.

The proof is in documentation.

Did you start your business in 2018?

All of the costs you incurred before the business began are considered to be "start-up costs". You can choose to deduct up to \$5,000 of these costs in the first year. The remainder must be written off over a 15 year period. Remember to separate these costs from the rest of your expenses when you compile your records.

Don't forget the 1099s.

If you paid any person \$600 or more to perform services for your business, you need to give them a 1099-Misc. by the end of January. Failure to do so will result in loss of the deduction if you are audited and a penalty if filed late.

1099-K:

If your business does internet sales or accepts credit card payments, you may be issued a Form 1099-K. These 1099s will be issued to persons or businesses who generate \$20,000 or 200 or more sales. To avoid an audit, please include all 1099-Ks with your tax information.

Do you work at home?

You may qualify for the home office deduction if you use a portion of your home as your principal place of business, to store inventory, or to conduct substantial management or administrative activities. There can be no other fixed location where these activities could be done.

The office space still needs to be **used regularly and exclusively for business,**

however. Which means you can not have any other usage of the area whatsoever. Using your office for personal or investment reasons eliminates the deduction as far as the IRS is concerned, so be careful to keep your office space and computer usage exclusively business. Having a deductible home office means you can deduct all of your local business travel as described earlier, and you will not have to keep a log of computer usage because your computer will be used exclusively for business.

If you qualify for the deduction, you will need some additional information:

- Measure your exclusive business space and total area of your home. The resulting business percentage is then applied to the total of your household expenses.

- Gather the following information to calculate the deduction: Mortgage interest, taxes, insurance, association fees, general repairs, maintenance, utilities, garbage pickup, security, and rent paid.

You must also depreciate your home, so you will have to bring an accounting of the total investment in your property.

- Alternatively, you can use the simplified method to calculate your home office deduction. Simply multiply the total percent of exclusive business use square feet by \$5 (maximum \$1500).

You can use the organizer on the next two pages to help you prepare for your tax appointment. Keep in mind the IRS compliance requirements and focus on documentation.



BUSINESS INCOME & EXPENSE WORKSHEET

YEAR _____

NAME _____ Federal ID # _____

NAME OF BUSINESS _____

ADDRESS OF BUSINESS _____

BUSINESS ACTIVITY (Check all that apply): sales manufacturing service

PRODUCT SOLD OR SERVICE PERFORMED _____

How many months was this business in operation during the year? 12 Months OR From _____ To _____

How many hours during the year did you and/or your spouse devote to this business? FULL TIME OR # of hours _____

Is any portion of your investment in this business *not* subject to payback by you? YES NO

▼ BUSINESS INCOME ▼

GROSS SALES/RECEIPTS	Include all 1099 income for services performed		1099 – MISC. Bring in ALL 1099s received. Include Non-Employee Amount in Gross Sales. Do your records agree with the amount reported? YES <input type="checkbox"/> NO <input type="checkbox"/> Did you receive \$10,000.00 in actual cash from any individual at any one time— <i>or in accumulated amounts</i> — during this tax year?
SALES TAX COLLECTED	If not included in above		
RETURNS / REFUNDS	Amount included in Gross Sales that was refunded to your client		
OTHER INCOME	Directly related to your business		

▼ Sales of Equipment, Machinery, Land, Buildings Held for Business Use ▼

Kind of Property	Date Acquired	Date Sold	Gross Sales Price	Expenses of Sale	Original Cost

▼ BUSINESS EXPENSES (cost of goods sold) ▼

PURCHASE OF PRODUCT & SUPPLIES FOR RESALE		FREIGHT-IN	Shipping cost to receive product or materials, if not included in purchases
PERSONAL USE	Actual cost of items in purchases used by you or your family	OTHER COSTS	
◇ COST OF LABOR		INVENTORY AT END OF YEAR	
PURCHASE OF MATERIAL FOR JOBS	(construction or installation type)	How did you arrive at inventory value? Actual Cost <input type="checkbox"/> Other (explain) _____	

▼ CAR and TRUCK EXPENSES ▼

	VEHICLE 1	VEHICLE 2
Year and Make of Vehicle		
Date Purchased (month, date and year)◇		
Ending Odometer Reading (December 31)		
Beginning Odometer Reading (January 1)	–	–
Total Miles Driven (End Odo – Begin Odo)		
Total Business Miles (do you have another vehicle?)		
Total Commuting Miles		
Parking Fees and Tolls		
License Plates		
Interest		
<i>Continue below if you take actual expense (must use actual expenses if you lease)</i>		
Gas, oil, lube, repairs, tires, batteries, insurance, supplies, wash, wax, etc.		
Lease Costs		

▼ OFFICE in HOME ▼

Date Acquired Home
Total Cost
Cost Of Land
Cost Of Improvements
Sq. Footage Of Home
Sq. Footage Of Office Area
Rent Paid (If You Rent)
Interest
Taxes
Utilities/Garbage
Insurance
Repairs/Maintenance
Hours Used Per Week
Hours Worked Per Week

BUSINESS EXPENSES (continued)

<p>ADVERTISING/PROMOTION: Ads, business cards, greeting cards, etc.</p> <p>*COMMISSIONS & FEES PAID: Contract labor</p> <p>EMPLOYEE BENEFITS: Health insurance, company party, mileage reimbursements, etc.</p> <p>INSURANCE: Worker's comp, business liability (do not include auto/truck/health)</p> <p>INTEREST: Mortgage (on business bldg.): Paid to financial institution Paid to individual</p> <p>OTHER INTEREST: (do not include auto or truck) List life insurance loans separately Business only credit card</p> <p>*LEGAL & PROFESSIONAL: Attorney fees for business, accounting fees, bonds, permits, etc.</p> <p>OFFICE EXPENSE: Postage, stationery, office supplies, bank charges, pens, etc.</p> <p>PENSION/PROFIT SHARING: Employees only</p> <p>*RENT/LEASE: Machinery and equipment Other business property</p> <p>*REPAIRS & MAINTENANCE: Building, equipment, etc. (do not include auto or truck)</p> <p>SUPPLIES: Misc. (not included elsewhere) Small tools</p> <p>TAXES: Personal property Licenses (not auto/truck) Real estate of business building & land Sales tax (if included in gross sales) Payroll (your share Soc.Sec./Medicare)</p> <p>TRAVEL (number of nights away): City_____ Nights out ___ City_____ Nights out ___ City_____ Nights out ___ City_____ Nights out ___ City_____ Nights out ___ City_____ Nights out ___ City_____ Nights out ___ City_____ Nights out ___</p>	<p>EXPENSES (AWAY FROM HOME OVERNIGHT): Lodging Meals & tips (keep total separate from other costs) Convention fees Cruise ship convention/seminar Airplane or train fares Auto rental, taxis or bus fares Other (incidentals, laundry, etc.)</p> <p>MEALS & ENTERTAINMENT*: Sales lunches Gifts (limited to \$25 per individual or couple) *Entertainment (e.g. tickets) is not deductible for tax year 2018 and beyond Tickets to qualified charitable events</p> <p>UTILITIES & TELEPHONE: Electricity (business) Natural gas/heating fuel (business) Garbage, water, sewer (business) Telephone (bus. line, second line, other options) Business long distance (from home telephone) Faxes, paging svcs, cellular svcs</p> <p>WAGES: (bring your copy of W-2s/941s if they have been filed) Wages to spouse (subject to Soc.Sec. and Medicare tax) Children under 18 (not subject to Soc.Sec. and Medicare tax) Other</p> <p>OTHER EXPENSES (not listed elsewhere): Bank charges Courier services Dues & publications Education Fuel for equipment (not auto/truck) Laundry & cleaning Printing & copying Show Fees Shipping</p>
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EQUIPMENT PURCHASED

Item Purchased	Date Purchased	Business Use %	Cost (including sales tax)	Item Traded	Additional Cash Paid	Traded with Related Property	Other Information

*1099s: Amounts of \$600.00 or more paid to individuals (not corporations) for rent, interest, or services rendered to you in your business, require information returns to be filed by payer.

Due date of return is January 31. Nonfiling penalty may apply. If recipient does not furnish you with his/her Social Security Number, you are required to withhold tax on the payment(s).

Name	Address	Social Security #	Amount	Purpose of Payment