

# 2022 SMALL BUSINESS YEAR-END LETTER



## **New rules for form 1099-K... delayed**

The American Rescue Plan Act (ARPA) of 2021 changed the reporting threshold for 3rd party payment processors like Venmo, PayPal, CashApp, Square, etc. Under ARPA, the threshold for 2022 was reduced to \$600 (annual total, regardless of the number of business transactions). The IRS later announced that more time was needed to ensure that 1099-K forms would not be issued for personal transactions. Until further notice, the pre-ARPA reporting threshold of \$20,000 (and 200+ transactions) for “goods and services” will be the rule.

## **Is your business profitable?**

Profitable business owners (excluding C-corporation owners) with taxable income under \$340,100 (married) and \$170,050 (single) may get the **Qualified Business Income Deduction (QBIID)**. 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 the thresholds mentioned above will generally get to deduct 20% of Qualified Business Income (with some exceptions).

## **What is Qualified Business Income (QBI)?**

QBI is closely related to profit. If your business is profitable you likely will have QBI (with some exceptions).

**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.

In this example, Paul could have gotten a bigger deduction if his taxable income was higher. However, Paul would not want his taxable income to get too high. That's because the rules are less favorable if taxable income is above \$170,050/\$340,100 (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 QBIID.

Businesses that are NOT services (e.g. manufacturing, retail, etc.) can have taxable income above these levels and still get the deduction. However, their deduction is limited by other factors such as wages paid to employees and the value of certain business assets.

## **Does your business lose money?**

**Be aware of the hobby loss rules.** With the IRS hot on reducing revenue losses, be aware that your business could be reclassified as a hobby. 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. Hobby income is claimed in full and **expense deductions are not allowed**.

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 bank account and credit card for business.
- Keep a log of activity.
- Advertise

## **Did you pay for health insurance?**

A self-employed taxpayer can deduct the amount paid for medical insurance for him/herself, spouse, and dependents as an adjustment to income. Deductible payments for health insurance also include Medicare premiums. The deduction is limited to net income from self-employment. 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.

## **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 31<sup>st</sup>. The same deadline applies to 1099-NEC

filings for independent contractors.

If you purchased health insurance for your employees, you might qualify for a 2022 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 alternatively offer a Health Reimbursement Arrangement. Work with a service provider to manage the rules and complexities (including but not limited to HIPAA).

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

## **Employee Retention Credits (ERC)?**

The ERC was a payroll tax credit for businesses that retained employees despite revenue reductions or governmental shut-downs preventing them from doing business during the pandemic.

The ERC began on 3/13/20 and ran through 12/31/21. If you didn't get an ERC you can amend quarterly payroll tax filings to claim one now (only if you qualify, of course).

Initially, businesses were not allowed to claim both the ERC and a Paycheck Protection Program loan. However, Congress acted to allow both the ERC and PPP if they had greater than 20% quarterly revenue reductions (vs. the prior year or prior quarter). The details regarding ERC qualifiers are beyond the scope of this newsletter. Ask for help to see if you qualify (as mentioned above, payroll tax filings can be amended to claim an unclaimed ERC).

Unfortunately, the ERC reduces your business' allowable wage deductions (for the tax year that the credit was issued). As such, if you amend to claim an ERC you must also amend the corresponding income tax return.



### **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 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. There are two rates for 2022: 1/1—6/30 is 58.5¢ and 7/1—12/31 is 62.5¢ 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 nearby supplier can help increase deductible miles.

#### ***The proof is in documentation.***

#### **Meals and Entertainment:**

Don't forget that recent tax law changes eliminated the deduction for certain types of client entertainment. You can still deduct business meeting food & drink. However, tickets to events and most entertainment are no longer deductible. For example, if you hosted a business meeting at a baseball game the hotdogs, peanuts, and beer would be deductible but the tickets would not.

Business meals from restaurants remain 100% deductible for 2022. However, starting 1/1/23 they go back to 50% deductible (like it was prior to 2021).

Remember that ALL business deductions must be ordinary and necessary.

#### **Don't forget the 1099s:**

If you paid any person \$600 or more to perform services for your business, you need to give them form 1099-NEC 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.

#### **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 ▼

<b>GROSS SALES/RECEIPTS</b>	Include all 1099 income for services performed		<b>1099 FORMS</b> 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?
<b>SALES TAX COLLECTED</b>	If not included in above		
<b>RETURNS / REFUNDS</b>	Amount included in Gross Sales that was refunded to your client		
<b>OTHER INCOME</b>	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) ▼

<b>PURCHASE OF PRODUCT &amp; SUPPLIES FOR RESALE</b>		<b>FREIGHT-IN</b>	Shipping cost to receive product or materials, if not included in purchases
<b>PERSONAL USE</b>	Actual cost of items in purchases used by you or your family	<b>OTHER COSTS</b>	
<b>◇ COST OF LABOR</b>		<b>INVENTORY AT END OF YEAR</b>	
<b>PURCHASE OF MATERIAL FOR JOBS</b>	(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
<b>Year and Make of Vehicle</b>		
<b>Date Purchased (month, date and year)◇</b>		
Ending Odometer <b>Reading (December 31)</b>		
Beginning Odometer <b>Reading (January 1)</b>	—	—
<b>Total Miles Driven (End Odo – Begin Odo)</b>		
<b>Total Business Miles ( 1-1 through 6-30 / 7-1 through 12-31 )</b>	/	/
<b>Total Commuting Miles</b>		
<b>Parking Fees and Tolls</b>		
<b>License Plates</b>		
<b>Interest</b>		
<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.		
<b>Lease Costs</b>		

## ▼ OFFICE in HOME ▼

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

## BUSINESS EXPENSES (continued)

<p><b>ADVERTISING/PROMOTION:</b> Ads, business cards, greeting cards, etc.</p> <p><b>*COMMISSIONS &amp; FEES PAID:</b> Contract labor</p> <p><b>EMPLOYEE BENEFITS:</b> Health insurance, company party, mileage reimbursements, etc.</p> <p><b>INSURANCE:</b> Worker's comp, business liability (do not include auto/truck/health)</p> <p><b>INTEREST:</b>     <b>Mortgage</b> (on business bldg.):                              Paid to financial institution                              Paid to individual</p> <p><b>OTHER INTEREST:</b>                              (do not include auto or truck)                              List life insurance loans separately                              Business only credit card</p> <p><b>*LEGAL &amp; PROFESSIONAL:</b> Attorney fees for business, accounting fees, bonds, permits, etc.</p> <p><b>OFFICE EXPENSE:</b> Postage, stationery, office supplies, bank charges, pens, etc.</p> <p><b>PENSION/PROFIT SHARING:</b> Employees only</p> <p><b>*RENT/LEASE:</b>   Machinery and equipment                                    Other business property</p> <p><b>*REPAIRS &amp; MAINTENANCE:</b> Building, equipment, etc. (do not include auto or truck)</p> <p><b>SUPPLIES:</b>       Misc. (not included elsewhere)                                    Small tools</p> <p><b>TAXES:</b>        Personal property                              Licenses (not auto/truck)                              Real estate of business building &amp; land                              Sales tax (if included in gross sales)                              Payroll (your share Soc.Sec./Medicare)</p> <p><b>TRAVEL</b> (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><b>EXPENSES (AWAY FROM HOME OVERNIGHT):</b>          Lodging          Meals &amp; 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><b>MEALS &amp; ENTERTAINMENT*:</b>          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><b>UTILITIES &amp; TELEPHONE:</b>          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><b>WAGES:</b>       (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><b>OTHER EXPENSES</b> (not listed elsewhere):          Bank charges          Courier services          Dues &amp; publications          Education          Fuel for equipment (not auto/truck)          Laundry &amp; cleaning          Printing &amp; 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