IRS Guidance for Business Deductions & Credits

Small Business Week in the U.S. was May 5-11. The Internal Revenue Service issued news releases as guidance for small business owners and self-employed individuals as a reminder to take deductions and credits that will give them a more attractive bottom line and lower tax liability.

Business owners can estimate their tax situation to allow for planning ahead. A few significant deductions and credits that can be useful for small business taxpayers are presented here.

Deductions

Qualified business income deduction

Individuals, (including owners of sole proprietorships, partnerships, S corporations, trusts and estates) may be entitled for a *qualified business income deduction*, or the section 199A deduction. Some trusts and estates could claim the deduction directly as well.

The deduction allows business owners to deduct up to 20 percent of their qualified business income (QBI), plus 20 percent of qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income. Income earned by a C corporation or by providing services as an employee would not be eligible for the QBI deduction.

The deduction became available for the tax years beginning after December 31, 2017. Entitled taxpayers can declare it for the first time on the 2018 federal income tax returns filed in 2019.

Business losses

Under TCJA of 2017, losses from business are now limited to $250,000, or $500,000 for a joint tax return. The losses can be from activities reported on Schedule C by a self-employed individual, or farming activities reported on Schedule F. The losses can also come from being an employee as well of certain activities reported on Schedule E. However, excess business losses that are no longer allowed are treated as a net operating loss (NOL). These are to be carried forward to the next tax year.

However, most taxpayers with NOLs coming after 2017 are only allowed to carry forward. Certain farming businesses and insurance companies can still use a two-year carryback for certain losses. After Dec. 31, 2017, the net operating loss deduction is limited to 80 percent of the taxable income. The rules for existing or pre-2018 NOLs do not change.

Business expenses

In most cases, business expenses are deductible if the business operates for profit and the business expense must be both ordinary and necessary. An ordinary expense is common and accepted in the trade or business. A necessary expense is helpful and appropriate for the trade or business. An expense does not have to be essential to be considered obligatory. Business expenses can include:

- **Business use of a home** – If a taxpayer uses part of their home for business, part of their home expenses could be deductible. These expenses include mortgage interest, insurance, utilities, repairs and depreciation. Some expenses could be directly related to the business as well. Special rules and limits could apply. See the IRS Publication 587 for additional details.
- **Business use of a car** – A business owner using their car in their business can deduct car expenses. If it used for both business and personal purposes, a log must be kept dividing expenses based on actual mileage. For additional details, including special recordkeeping rules, see IRS Publication 463.
- **Meals and entertainment** – In general, businesses can deduct 50 percent of the cost of business meals if the taxpayer, or an employee, is present and the food or beverages aren't lavish or extravagant.
- **Rent expense** – In general, any business owner can deduct rent as an expense only if the rent is for property used in their trade or business. If they buying, or own, the property, then it is not deductible.
- **Interest** – Businesses may borrow money for their activities. The business interest expense can be deductible as well. In addition, limits and special rules may apply. See the IRS's page on Basic questions and answers about the limitation on the deduction for business interest expense for additional information.
- **Taxes** – A taxpayer can deduct most federal, state, local, and foreign taxes directly related to their trade or business as business expenses.

The IRS publishes Publication 535, Business Expenses, containing additional information about deductible business expenses, including employee related expenses such as employees' pay, retirement plans and insurance.

Credits

General business credits

The IRS allows general business credits which includes about two dozen tax credits for a variety of businesses and business activities. Often, a business taxpayer that can qualify for one or more of these credits but is unable to take them for a given tax year can carry them back to a prior year or forward to future years. See IRS Form 3800 and its instructions for details.

Employer credit for paid family and medical leave

The TCJA included a new general business credit that qualified employers may claim based on wages paid to qualifying employees for family and medical leave. To claim the credit, eligible employers must have a written policy in place that meets IRS requirements. Some of these requirements include providing at least 2 weeks of paid leave to full-time employees, or prorated for part-time employees, and the paid leave must be at least 50 percent of the wages normally paid to the employee. For TY 2018, the employee's prior year compensation from the employer must have been $72,000 or less. See Notice 2018-71 and instructions for IRS Form 8994 for details.

Tax credits can help employers hiring new workers

With the tight job market, business can possibly take advantage of another general business credit. The Work Opportunity Tax Credit (WOTC) is intended to help employers who hire long-term unemployment recipients, certain veterans, recipients of public assistance and other categories of workers with employment barriers. Certification requirements and other special rules apply. To find out more, visit IRS.gov/wotc.

Find more information about business tax credits on IRS.gov.

EINs – Rules Changes

Beginning May 13, the IRS announced the change in the rules to obtaining EINs. The changes allow only individuals with tax identification numbers, (either a Social Security number (SSN) or an individual taxpayer identification number (ITIN)), to request an employer identification number (EIN). This new requirement, was first announced by the IRS in March, will provide greater security to the EIN process by requiring an individual to be the responsible party and will also improve transparency. An EIN is a nine-digit tax identification number assigned to sole proprietors, corporations, partnerships, estates, trusts, employee retirement plans and other entities for tax-filing and reporting purposes.

The change prohibits entities from using their own EINs to obtain additional EINs thus reducing fraudulent businesses. The new requirement applies to both the paper Form SS-4, Application for Employer Identification Number (PDF), and online EIN applications.

Data security

The Internal Revenue Service warns of various methods of scams occurring with identify theft with individuals plus also filings of tax returns of businesses of Forms 1120, 1120S or Schedule K-1. The IRS reported that last year, 2,450 businesses reported that they were victims of tax-related identity theft, a 10-percent increase over 2017.

The IRS has several publications or methods to report any fraudulent activity or procedures for protection. More information from the IRS includes: Publication 4524, Taxes. Security. Together: Security Awareness for Taxpayers (PDF), or beware of phishing emails, (the most common tactic used by criminals to steal data). See Form W-2/SSN Data Theft: Information for Businesses and Payroll Service Providers. For additional protection of data see the IRS Publication 4557, Safeguarding Taxpayer Data (PDF).

Contact Mir Taxes LLC for additional information.