

Home Business Tax Deductions

19th Edition

Stephen Fishman, J.D.

Table of Contents

Chapter 1 – Some Tax Basics	1
Learning Objectives	1
Introduction.....	1
How Tax Deductions Work.....	1
Types of Tax Deductions	1
You Pay Taxes Only on Your Business Profits	2
Claiming Your Deductions.....	2
Make Sure You Are in Business.....	2
How Businesses Are Taxed	2
Basic Business Entities.....	3
Sole Proprietorship – The Most Popular Home Business Entity	3
Tax Treatment	4
What Businesses Can Deduct.....	5
Start-Up Expenses.....	5
Operating Expenses	5
Capital Expenses.....	5
Pass-Through Tax Deduction.....	6
Inventory.....	6
Adding It All Up: The Value of Tax Deductions	6
Federal and State Income Taxes	6
Self-Employment Taxes.....	7
Total Tax Savings	8
Businesses That Lose Money	8
What Is an NOL?	8
NOLs for 2017 and Earlier	8
NOLs for 2018 Through 2020.....	9
NOLs for 2021 and Later.....	9
Annual Dollar Limit on NOL Deduction	9
Claiming an NOL Refund	10
Review Questions.....	11
Review Answers	12
Chapter 2 – Is Your Home Business Really a Business?	13
Learning Objectives	13
Introduction.....	13
Proving That You Are in Business	13
Profit Test.....	14
Behavior Test	15
Tax Consequences of Engaging in a Hobby.....	18
Investing and Other Income-Producing Activities.....	18
Tax Consequences of Income-Producing Activities	19
Medicare Tax on Investment Income.....	19
Types of Income-Producing Activities.....	20
Trading in Stocks as a Business	20
Trading in Crypto as a Business.....	21
Review Questions.....	22
Review Answers	23
Chapter 3 – Getting Your Business Up and Running	25
Learning Objectives	25
Introduction.....	25
What Are Start-Up Expenses?	25
Common Start-Up Expenses.....	26
Special Rules for Some Expenses	26

Table of Contents

Buying an Existing Business	27
Expanding an Existing Business	27
When Does a Business Begin?	27
If Your Business Doesn't Last 15 Years	27
Expenses for Businesses That Never Begin.....	28
General Start-Up Costs.....	28
Costs to Start or Acquire a Specific Business.....	28
Avoiding the Start-Up Tax Rule's Bite	28
Review Questions.....	30
Review Answers	31
Chapter 4 – Home Business Operating Expenses	33
Learning Objectives	33
Introduction.....	33
Requirements for Deducting Operating Expenses	33
Ordinary and Necessary	33
Current Expense.....	35
Business Related.....	35
Reasonable in Amount.....	36
Operating Expenses That Are Not Deductible	36
Operating Expenses Paid With Paycheck Protection Program Loans	37
Forgiven PPP Loans Are Tax-Free.....	37
Deductions for Expenses Paid With Forgiven PPP Loans.....	37
How to Report Operating Expense Deductions.....	38
Review Questions.....	39
Review Answers	40
Chapter 5 – Deducting Long-Term Assets	41
Learning Objectives	41
Introduction.....	41
Long-Term Assets	41
Deducting Inexpensive Property: The De Minimis Safe Harbor and Materials and Supplies	
Deduction	42
The De Minimis Safe Harbor	42
Maximum De Minimis Amount.....	43
The Materials and Supplies Deduction	45
Interaction With De Minimis Safe Harbor.....	45
General Rules for Deducting Long-Term Personal Property	45
What You Can Deduct	46
Disposing of Long-Term Assets	48
Bonus Depreciation	49
Property That Qualifies for Bonus Depreciation	49
Calculating the Bonus Amount	50
Class-Wide Requirement	50
Opting Out of the Bonus.....	50
Bonus Depreciation Percentages	51
Section 179 Deductions	51
Deducting Repairs and Improvements.....	52
Regular Depreciation	52
When to Use Regular Depreciation	52
Depreciation Period	53
Depreciation Methods	53
Depreciation Rules for Listed Property	55
Real Property.....	55
Deducting Business Vehicles	56
Is Your Vehicle a Passenger Automobile?.....	56
Annual Depreciation Limits for Passenger Automobiles.....	56

Table of Contents

Heavy Deductions for Heavy Metal: Bonus Depreciation for SUVs and Other Weighty Vehicles	57
Tax Reporting and Record Keeping	57
Leasing Long-Term Assets	58
Review Questions	60
Review Answers	62
Chapter 6 – The Home Office Deduction	65
Learning Objectives	65
Introduction.....	65
Qualifying for the Home Office Deduction.....	65
Threshold Requirements: Regular and Exclusive Business Use	67
Additional Requirements	69
Corporation Employees.....	72
Calculating the Home Office Deduction	73
How Much of Your Home Is Used for Business?	73
What Expenses Can You Deduct?	76
Simplified Home Office Deduction Method	82
How the Simple Method Works	82
IRS Reporting Requirements	83
Audit-Proofing Your Home Office Deduction.....	84
Prove That You Are Following the Rules	84
Keep Good Expense Records.....	84
Review Questions.....	85
Review Answers	87
Chapter 7 – The Pass-Through Tax Deduction	89
Learning Objectives	89
Introduction.....	89
You Must Have a Pass-Through Business	89
You Must Have Qualified Business Income	90
You Must Have Taxable Income	90
Deduction for Taxable Income Up to \$170,050 (\$340,100 if Married).....	91
Deduction for Income Above \$170,050 (\$340,100 if Married)	91
Are You a Specified Service Business?.....	91
Deduction for Non-Service Businesses (Income Above \$170,050/\$340,100).....	92
Deduction for Specified Service Business Owners (Income Above \$170,050/\$340,100)	93
Taking the Pass-Through Deduction	94
Strategies to Maximize the Pass-Through Deduction.....	94
Keep Service Business Income Below \$220,050/\$440,100 Threshold	94
Form an S Corporation	94
Combine Multiple Non-Service Businesses	95
File a Separate Return.....	96
Review Questions.....	97
Review Answers	98
Chapter 8 – Getting Around Town: Car and Local Travel Expenses.....	99
Learning Objectives	99
Introduction.....	99
Deductible Local Transportation Expenses.....	99
Travel Must Be for Business	99
Trips from Your Home Office.....	100
If You Have No Regular Workplace.....	100
The Standard Mileage Rate	101
How the Standard Mileage Rate Works.....	101
Requirements to Use the Standard Mileage Rate.....	102
The Actual Expense Method	102
How the Actual Expense Method Works.....	102

Table of Contents

Record-Keeping Requirements	103
Vehicle Depreciation Deductions	103
Leasing a Car	104
Other Local Transportation Expenses	104
Reporting Transportation Expenses on Your Tax Return	104
Sole Proprietors	104
LLCs and Partnerships	105
Corporations	105
When Clients or Customers Reimburse You	105
Review Questions	106
Review Answers	107
Chapter 9 – Leaving Town: Business Travel.....	109
Learning Objectives	109
Introduction.....	109
What Is Business Travel?	109
Where Is Your Tax Home?.....	110
Your Trip Must Be for Business	112
Deductible Travel Expenses.....	113
Traveling First Class or Steerage	114
Taking People with You	114
How Much You Can Deduct.....	114
Travel Within the United States	115
Travel Outside the United States.....	115
Conventions	116
Travel by Ship.....	117
Calculating Time Spent on Business	118
Limits on Meal Expense Deduction	118
Maximizing Your Business Travel Deductions	120
Plan Ahead.....	120
Make a Paper Trail	120
Maximize Your Business Days.....	120
Take Advantage of the Sandwich Day Rule.....	121
Travel Expenses Reimbursed by Clients or Customers	121
Review Questions.....	122
Review Answers	123
Chapter 10 – Inventory	125
Learning Objectives	125
Introduction.....	125
What is Inventory?	125
Supplies Are Not Inventory	125
Incidental Supplies.....	126
Long-Term Assets	126
Deducting Inventory Costs	126
Nonincidental Materials and Supplies Deduction	126
Books and Records Deduction for Inventory.....	127
Maintaining an Inventory	128
Determining the Value of Inventory	128
Review Questions.....	131
Review Answers	132
Chapter 11 – Hiring Help: Employees and Independent Contractors	133
Learning Objectives	133
Introduction.....	133
Employees Versus Independent Contractors.....	133
Tax Deductions and Credits for Employee Pay and Benefits	135

Table of Contents

Payroll Taxes.....	135
State Payroll Taxes.....	137
Employee Fringe Benefits.....	138
COVID-Related Employer Tax Credits.....	139
Employing Your Family or Yourself.....	139
Employing Your Children.....	139
Employing Your Spouse.....	141
Rules to Follow When Employing Your Family.....	141
Employing Yourself.....	143
Tax Deductions When You Hire Independent Contractors.....	144
No Deductions for ICs' Taxes.....	144
Paying Independent Contractors' Expenses.....	145
Review Questions.....	146
Review Answers.....	147
Chapter 12 – What if You Get Sick? Deducting Medical Expenses.....	149
Learning Objectives.....	149
Introduction.....	149
The Affordable Care Act (ACA).....	149
Federal Individual Health Insurance Mandate Terminated.....	149
The Employer Mandate.....	150
ACA Health Insurance Rules.....	150
State Health Insurance Exchanges.....	151
Open Enrollment Periods.....	151
Health Insurance Premium Tax Credits.....	152
The Personal Deduction for Medical Expenses.....	153
Deducting Health Insurance Premiums.....	153
Personal Income Tax Deduction for the Self-Employed.....	153
Deducting Health Insurance as a Business Expense.....	155
Sick and Family Leave Tax Credits for the Self-Employed.....	157
Tax Credits for Employee Health Insurance.....	157
Health Reimbursement Arrangements.....	157
Spousal Health Reimbursement Arrangements.....	158
What Expenses May Be Reimbursed?.....	159
How to Establish a Spousal HRA.....	159
Sample Spousal HRA.....	159
Individual Coverage HRAs (ICHRAs).....	161
Qualified Small Employer HRAs (QSEHRAs).....	162
Health Savings Accounts.....	163
What Are Health Savings Accounts?.....	163
Establishing Your HSA.....	163
Making Contributions to Your HSA.....	164
Withdrawing HSA Funds.....	165
Are HSAs a Good Deal?.....	166
HSAs for Employees.....	166
Tax Reporting for HSAs.....	167
Review Questions.....	168
Review Answers.....	169
Chapter 13 – Deductions That Can Help You Retire.....	171
Learning Objectives.....	171
Introduction.....	171
Why You Need a Retirement Plan (or Plans).....	171
Tax Deduction.....	172
Tax Deferral.....	172
Individual Retirement Accounts (IRAs).....	172
Traditional IRAs.....	173

Table of Contents

Roth IRAs.....	174
Employer IRAs.....	175
SEP-IRAs.....	175
SIMPLE IRAs.....	175
Keogh Plans.....	176
Types of Keogh Plans.....	176
Setting Up a Keogh Plan.....	177
Withdrawing Your Money.....	177
Solo 401(k) Plans.....	177
Review Questions.....	179
Review Answers.....	180
Chapter 14 – More Home Business Deductions.....	181
Learning Objectives.....	181
Introduction.....	181
Advertising.....	181
Goodwill Advertising.....	181
Giveaway Items.....	182
Website Development and Maintenance.....	182
Business Bad Debts.....	182
Requirements to Deduct Bad Debts.....	182
Types of Bad Debts.....	184
Casualty Losses.....	185
Amount of Deduction.....	186
Damage to Your Home Office.....	187
Tax Reporting.....	188
Charitable Contributions.....	188
Dues and Subscriptions.....	189
Education Expenses.....	189
Starting a New Business.....	190
Minimum Educational Requirements.....	190
Traveling for Education.....	190
Entertainment and Meals.....	191
Entertainment.....	191
Meals.....	191
Gifts.....	193
Insurance for Your Business.....	193
Homeowners' Insurance for Your Home Office.....	194
Car Insurance.....	194
Interest on Business Loans.....	194
Home Offices.....	194
Car Loans.....	194
Loans from Relatives and Friends.....	195
Loans to Buy a Business.....	195
Interest You Can't Deduct.....	195
Deducting Investment Interest.....	195
Legal and Professional Services.....	196
Buying Long-Term Property.....	196
Starting a Business.....	196
Accounting Fees.....	196
Taxes and Licenses.....	196
Income Taxes.....	196
Self-Employment Taxes.....	197
Employment Taxes.....	197
Sales Taxes.....	197
Real Property Taxes.....	197
Other Taxes.....	198

Table of Contents

License Fees	198
Review Questions	199
Review Answers	200
Chapter 15 – Using Cryptocurrency in Your Business	201
Learning Objectives	201
Introduction.....	201
What Is Cryptocurrency?.....	201
Why You Might Want to Use Cryptocurrency in Your Business.....	201
Tax Treatment of Cryptocurrency.....	202
Accepting Cryptocurrency as Payment for Services	202
Accepting Cryptocurrency as Payment for Goods.....	203
Using Cryptocurrency to Pay for Business Expenses	203
Paying Independent Contractors with Cryptocurrency	203
IRS Reporting of Cryptocurrency Transactions.....	203
Record Keeping for Cryptocurrency Transactions.....	204
Accounting for Cryptocurrency Transactions	204
How to Report Cryptocurrency Revenue to the IRS.....	205
Cryptocurrency Tax Treatment Guide	205
Review Questions.....	206
Review Answers	207
Chapter 16 – Record Keeping and Accounting.....	209
Learning Objectives	209
Introduction.....	209
What Records Do You Need?	209
Business Checkbook and Credit Cards	209
Records of Your Income and Expenses	212
Paper Versus Electronic Records.....	212
Create Your Own Spreadsheet	212
Personal Finance Software	212
Small Business Accounting Software	213
Online Bookkeeping.....	213
Tracking Your Business Expenses	213
Supporting Documents	215
Records Required for Specific Expenses	217
Automobile Mileage and Expense Records	217
Travel and Gift Expenses.....	219
Listed Property	221
How Long to Keep Records	221
What If You Don't Have Proper Tax Records?.....	222
Accounting Methods	222
Cash Method	223
Accrual Method.....	225
Tax Years.....	225
Review Questions.....	226
Review Answers	227
Chapter 17 – Businesses Owned By Spouses	229
Learning Objectives	229
Introduction.....	229
An Employer-Employee Arrangement	229
Social Security Tax Savings.....	229
Bona Fide Employee Requirement.....	230
Reasonable Compensation Requirement.....	230
Your Spouse Won't Qualify for Social Security? So What!	230
What About Limited Liability?	231

Table of Contents

Establish a Qualified Joint Venture.....	231
Qualifying for QJV Status.....	231
Community Property Sole Proprietorships.....	231
Form a Business Entity.....	232
Do Nothing.....	232
Review Questions.....	233
Review Answers.....	234
Chapter 18 – Nine Tips for Avoiding an IRS Audit.....	235
Learning Objectives.....	235
Introduction.....	235
Tip #1: Be Thorough and Exact.....	235
Tip #2: Don't File Early.....	235
Tip #3: File Electronically.....	235
Tip #4: Form a Business Entity.....	235
Tip #5: Explain Items the IRS Will Question.....	236
Tip #6: Avoid Ambiguous or General Expenses.....	236
Tip #7: Report All of Your Income.....	236
Tip #8: Watch Your Income-to-Deduction Ratio.....	236
Tip #9: Beware of Abnormally Large Deductions.....	236
Review Questions.....	237
Review Answers.....	238
Glossary.....	239
Index.....	243