

Deductible Business Expenses for Business Owners

by: Wray Rives CPA CGMA

wray@NeedaCPA.com

I am frequently asked by business owners, "Give me a comprehensive list of business deductions, I don't want to miss any possible deductions." The truth is there is no way to make a comprehensive list of business expenses, because every business is unique and what may be a totally legitimate deduction for one business might not be a deduction for another type of business. The IRS defines business expense deductions as any expenditure that is normal and necessary to operate your business. That is a pretty broad definition. While I cannot give you a comprehensive list of deductions, what I can do is give you some categories to think about when you considering what is a normal and necessary expense to operate your business.

Cost of goods-If you sell a product this would represent anything that goes into actually making the product sellable. Things like materials, components, supplies that are used in the manufacturing process. Labor to manufacture or assemble the product. Packaging supplies required to package your product. If you are in the business of selling a service, it is perfectly normal to not have any cost of goods sold, but if you sell a tangible product, you likely do have cost of goods.

Advertising and Promotion-Expenses to advertise your business and help attract customers and clients. Marketing, promotional literature, gifts for customers and online ads would be examples.

Auto and vehicle expense-If you use your car for business purposes this one can be tricky, because you are required to choose between taking a deduction for the actual expenses or keeping track of your mileage and taking the standard mileage deduction that is published by the IRS. If you own the vehicle you must use the standard mileage rate the first year it is placed in service to continue using the standard mileage deduction or if you lease the vehicle, you must use the standard mileage deduction for every year of the lease term. You cannot use actual expense method for a leased vehicle if you previously used the standard mileage rate method. You must use the actual expenses if you have more than 5 business vehicles. The standard mileage rate replaces all operating cost of the vehicle including gas, oil, maintenance, depreciation, interest and licenses. If you use the standard mileage rate, you can add in actual expense for tolls and parking.

Commissions & Fees-Expense paid to other businesses to bring sales to your business.

Contract Labor-Contract labor includes payments to independent contractors who provide services to your business. You must use Form 1099-Misc to report payments that total more than \$600 to any US based individual during the year. This reporting is due in January of each calendar year.

Depreciation-You are allowed a deduction for depreciation expense on business assets that you purchase. Many businesses may qualify for what are known as bonus depreciation and Section 179 depreciation deductions that may allow you to write off the full cost of a capital asset in the first year. You must file a Form 4562 to report depreciation on any assets placed in service in the current year or depreciation on any “listed property”. Listed property are a special category of assets that commonly have both business and personal use. The most common listed property are cars, trucks, motorcycles, cameras and computers and computer related equipment.

Wages and payroll expense-You can take a deduction for salaries or wages paid to employees of your business. You also can deduct employee benefit costs including pensions and retirement benefits and payroll taxes paid by your business.

Interest expense-You can deduct interest expense paid by your business, but see the discussion of Home Office Expenses below for specifics on interest for your home.

Rental and lease payments-You can deduct payments to rent vehicles, facilities and equipment for your business.

Insurance-You can deduct insurance payments made for the business.

Professional and legal services-Expenses paid to attorneys, accountants and other professionals for services provided to your business are deductible. See the note regarding 1099-Misc reporting discussed in the contract labor category above.

Office expense and supplies-Expenses to operate your business such as paper, ink and other types of supplies are deductible. You can deduct the cost of books, professional instruments and tools if you typically use those items up in one year.

Repairs and maintenance-Payments to maintain and repair business assets are deductible. If you make significant improvements to an asset then the payments might need to be considered a capital expenditure.

Taxes and Licenses-Any payments for business tax or a business license is a deductible expense. If you charge sales tax, you should either reduce your revenue by the amount of sales tax paid or you may prefer to just take a deduction for the sales tax that you pay and include the sales tax collected in your revenue. Other deductible taxes might include property tax on business assets, highway use tax or unemployment taxes. You should note that penalties paid in addition to the taxes are typically not deductible.

Travel and meals expense-Necessary travel expense for your business is deductible. You can deduct the actual cost or you can use the federal per-diem rates for travel and meals expense. Self-employed individuals cannot use the per-diem rates for their own lodging expense, but must report the actual expenditure. Meals expense are limited to 50% of the actual cost as the deductible amount. Individuals who are subject to federal transportation regulations may be able to deduct a greater percentage for meals. Expenditures for catered events for customers and/or employees may be deductible at 50%. There are special rules that must be followed for travel outside of North America. You cannot deduct expenses for travel for your spouse or dependent unless that person is your employee and their travel is for a bona fide business purposes. For tax years beginning after 12/31/2017, entertainment expenses are no longer deductible as a business expense.

Utilities-Items like electricity, gas and water are deductible if they are incurred for your business. See the discussion below about home office deductions for the business use of your home if you are self-employed.

Home Office Expenses-There is a special deduction for self-employed individuals. If you use a portion of your home exclusively for your business, you may be able to deduct a proportion of the expenses to maintain and operate your home as a home office deduction. To take the home office deduction, you will need to file a Form 8829 to calculate the amount of home office deduction you are entitled to. The home office deduction includes all the expenses of your home including interest, property taxes, utilities, repairs, cleaning and maintenance. You can also take a depreciation deduction for the portion of your home that is used for the business.

As I mentioned at the beginning, there is really no way to cover a comprehensive list of deductions every business. The US tax courts have in fact allowed several somewhat unusual tax deductions as business expenses including:

1. Breast implants for an exotic dancer.
2. Cost of beer given to customers of a convenience store.
3. Cost of cat food for a junk yard owner.
4. Body oil for a professional body builder.
5. A portion of the money paid to a live-in girlfriend

The best thing you can do is keep track of any expense you think “might” be a tax deduction and then discuss the expenditure with us before preparing your tax return. We can help you answer the question if something is a legitimate deduction for your business.