SAPPHIRE BOOKKEEPING & TAX SOLUTIONS LLC

NEWSLETTER

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EDITION 4

WELCOME TO OUR QUARTERLY NEWSLETTER, DEDICATED TO PROVIDING SMALL BUSINESS OWNERS WITH VALUABLE INSIGHTS AND STRATEGIES TO OPTIMIZE THEIR TAX SAVINGS. IN EACH EDITION, WE'LL SHARE EXPERT TIPS, PRACTICAL ADVICE, AND UPDATES ON TAX LAWS AND REGULATIONS TO HELP YOU NAVIGATE THE COMPLEXITIES OF THE TAX CODE WITH CONFIDENCE.

READ ON AS WE EXPLORE INNOVATIVE TAX-SAVING STRATEGIES, DEBUNK COMMON MYTHS, AND PROVIDE GUIDANCE TAILORED TO THE UNIQUE NEEDS OF SMALL BUSINESSES.

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512.522.2340

SapphireTaxSolutions.com

info@sapphiretaxsolutions.com

IS YOUR BUSINESS JUST A HOBBY IN THE EYES OF THE IRS?

The IRS often looks at the nature of business activities to distinguish between what is genuinely a business and what might be a hobby, primarily to claim unjustified tax deductions. Here are some common red flags the IRS looks for when determining if your business might actually be considered a hobby:

1.Lack of Profit: If your activity isn't profitable, especially if it fails to generate profit in at least three out of the last five consecutive years, the IRS might classify it as a hobby. This is often referred to as the "hobby loss" rule.

2. Expertise of the Taxpayer: The IRS considers whether or not you have the necessary knowledge or expertise to turn the activity into a successful business. Lack of such expertise could suggest the activity is more of a hobby.

3. Time and Effort Spent: If you don’t spend much time on the activity, it might appear to be a hobby. Businesses generally require substantial personal effort and regular involvement.

4. How the Activity is Carried Out: How you carry out the activity can also be indicative. If the activity is conducted in a businesslike manner, which includes keeping accurate books, records, and actively marketing one's services or products, it's more likely to be seen as a business.

5. Expectation of Asset Appreciation: If the assets used in the activity (such as land, horses, artwork) are expected to appreciate in value, this might suggest the activity is an investment rather than a business or hobby.

IS YOUR BUSINESS JUST A HOBBY IN THE EYES OF THE IRS? (CONT.)

6. Success in Other Similar Activities: If you have turned other similar activities into profitable ventures, this could indicate you have a business motive.

7. History of Income or Losses: A pattern of generating losses year after year might suggest the activity is not conducted with a profit motive. However, startup businesses often face initial losses.

8. Amount of Occasional Profits: Infrequent, small profits, when compared to larger consistent losses, might indicate that the activity is not engaged in for profit.

9. Financial Status of the Taxpayer: If you have substantial income from other sources, the IRS may scrutinize the activity more closely, particularly if losses generated from the activity serve to offset this other income.

10. Pleasure or Recreation: If the activity is enjoyable or recreational, the IRS might scrutinize whether this pleasure is the primary motive rather than earning a profit.

Understanding these factors can help ensure that your business operations clearly demonstrate a profit motive, which is crucial for tax reporting and compliance.

FROM GAILO'S DESK: WHAT IS A W-9 AND WHY SHOULD I CARE?

As a self employed business owner there are reporting responsibilities you have to the IRS that you may not be aware of if you are just starting out. Do you plan to hire a free-lance web designer to help with your website, a virtual assistant or some other type of contractor to provide a service to you, or maybe you pay rent for your office space? You may need to have them fill out a W-9 form in the event you end up making payments to them of $600 or more in a calendar year. The W-9 is specifically used for non-employee contractors (similar to how a W-4 is used for employees).

Our advice is to collect these forms as needed rather than wait until tax time. A W-9 collects the necessary information in order for you to issue a 1099 which is mandatory to send if the requirements are met. Any payments made by cash, check or cash equivalent (bank transfer or Zelle) to a contractor for $600 or more in a year require that you file an appropriate 1099 with the IRS by January 31 of the following year. Penalties can be assessed for each required form that is not filed.

If you fail to collect the W-9 form and willingly do not file a required 1099, you could be responsible for as much as 24% tax on the payments you made to that contractor. Do you want to pay someone else's taxes for them? I didn't think so!

OUR REFERRAL PARTNERS

We LOVE BlueVine! Not only do they offer 2% interest, they also make it so easy for our clients to provide true Accountant Access for us. We get read-only permissions and never have to bother you to send us a statement again! You can also pay vendors and set up ACH payments!

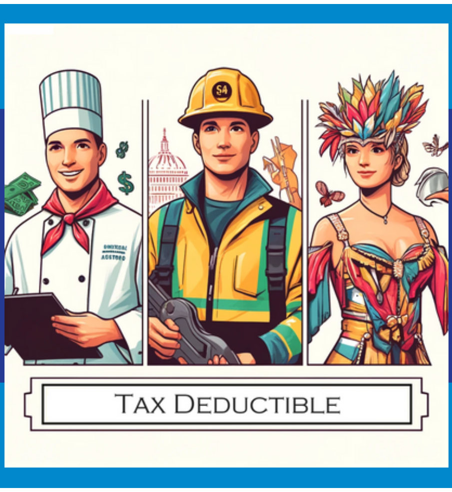
401GO is our choice when it comes to setting up 401Ks for our (and your!) business. You can set it up on your own or we can help! There is a tax credit available, and these contributions reduce your taxable income! Not to mention you are saving for your retirement. WAY TO GO!

TAX TALK: CAN I DEDUCT CLOTHING PURCHASES ON MY BUSINESS TAX RETURN?

As a seasoned tax preparer, one of the questions I encounter most frequently from business owners and professionals is: "Can I deduct clothing purchases on my business tax return?" It's a great question and the answer can significantly impact your tax situation. Below will outline the essentials of what you need to know about deducting clothing expenses.

The General Rule: Since the Tax Cuts and Jobs Act of 2018, the quick answer is NO. Clothing Must Be Exclusively for Work.

The IRS stipulates that clothing can only be deducted if it is both "ordinary and necessary" for your business and not suitable for everyday wear. This means the clothes must be specifically required for your work and not appropriate for personal use.



Examples of Deductible Clothing

- **Uniforms:** If your business requires you to wear a uniform that identifies you as an employee or a member of that business and it's not suitable for everyday use, this cost is deductible. Examples include police uniforms, health care scrubs, or mechanic coveralls. However, if you are an employee, these are no longer deductible. So only the purchase of uniforms by the business is deductible and in general, these must also include the business name screen printed or embroidered on them.
- **Protective Clothing:** Items necessary for protection at work, such as safety boots, hard hats, and goggles, are deductible. These are considered essential for carrying out the job safely and are typically not worn outside of work.
- **Costumes:** If you are in a profession where you need costumes (for example, entertainers or certain types of promoters), these can be deductible. These are considered necessary for performing your job and are not suitable for ordinary wear.

TAX TALK: CAN I DEDUCT CLOTHING PURCHASES ON MY BUSINESS TAX RETURN? (CONT.)

Non-Deductible Clothing

Most other types of clothing, even if purchased exclusively for work, do not qualify for a deduction. For instance, a business suit, while possibly bought for the purpose of looking professional at business meetings, is not deductible because it can also be worn for non-business occasions. The same applies to clothes bought for photo shoots, branding events and most other types of business casual wear.

Special Considerations

- Documentation: Keeping receipts and a detailed log of clothing purchases for work, including the specific reason why such clothing is required for your job, can be crucial in case of an IRS audit.
- Laundry and Upkeep: Costs for the cleaning and upkeep of deductible clothing (like uniforms or protective gear) can also be deductible. Ensure you keep detailed records of these expenses as well.

Final Thoughts

While the desire to maximize deductions is understandable, it's crucial to adhere closely to IRS guidelines to avoid complications. Deducting non-eligible attire can lead to an audit or additional taxes and penalties. When in doubt, consult with a tax professional who can provide guidance based on your specific circumstances and keep you compliant with tax laws.

Remember, every deduction you claim must be both ordinary (common and accepted in your field of business) and necessary (helpful and appropriate for your business). If your clothing purchase doesn't meet these criteria, it's safer to err on the side of caution and not claim it as a deduction.

By understanding and following these guidelines, you can ensure that your tax filings are accurate and maximize your legally entitled deductions without risking trouble with the IRS.

WHAT IS THE CTA AND THIS BOI REPORT I KEEP HEARING ABOUT?

The Corporate Transparency Act, or CTA, was enacted on January 1, 2021. It is an expansion of anti-money laundering laws and is intended to help prevent and combat money laundering, terrorist financing, corruption, tax fraud, and other illicit activity.

What does that mean for me?

This new law will require most existing and new corporate entities in the United States to file reports with the federal government regarding their beneficial owners- also referred to as the BOI Report (Beneficial Owner Information Report). These reports will be filed with the Department of the Treasury's Financial Crimes Enforcement Network, or FinCEN.

Who is required to file?

Every corporation, LLC or other entity created by the filing of a document with a Secretary of State or similar office under the law of a state or Indian tribe is required to file a BOI report unless it qualifies for an exemption. Those entities created in the United States and not exempt, and therefore required to file a BOI report, are called "domestic reporting companies". Certain entities created in foreign countries and registered to do business in the United States are also required to file a BOI report and are called "foreign reporting companies."

What is the deadline to file the BOI Report?

- Businesses established prior to January 1, 2024 have until December 31, 2024 to file the required reports.
- Businesses established on January 1, 2024 or later have 30 days to file the required reports.

What is the penalty if I don't complete this new reporting requirement?

In the event of willful violations (by intentional act or omission), companies could be subject to civil penalties of up to $500 per day of a continuing violation and further criminal penalties of up to $10,000 and imprisonment for up to two years.

We love our clients! Referrals are always appreciated!

IMPORTANT!!
BUSINESS OWNER REMINDERS

Remember that Quarter 2 is a short one… The IRS deadline for Q2 Estimated payments is JUNE 17, 2024. We call it "IRS Q2" and it is only 2 months long. Your quarterly payment should reflect your income from April and May.

If you start a business in 2024 and fall under the Corporate Transparency Act requirements for BOI Reporting, you only have 30 days to complete this report! See our CTA article above for more information.