



Small Business Deductions Letter

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Congratulations on starting your new business! As you get up and running, I wanted to provide you with a comprehensive checklist to help you stay on top of your federal tax responsibilities and ensure you're taking advantage of all the deductions available to small business owners. Please review the following information and let me know if you have any questions or would like to discuss any items in more detail.

Business Setup & Compliance

- Choose your business structure (sole proprietorship, partnership, corporation, S corporation, or LLC), as this will determine your tax filing requirements.
- Obtain an Employer Identification Number (EIN) if you have employees or need to file certain tax returns.
- Register for any required state and local taxes.
- Open a separate business bank account to keep your finances organized.
- Set up a recordkeeping system to track all income, expenses, and supporting documents (receipts, invoices, bank statements, etc.).

Accounting & Tax Year

- Select an accounting method (cash or accrual). Most small businesses use the cash method.
- Choose a tax year (calendar year is most common).

Filing & Payment Obligations

- File your annual income tax return (Form 1040 with Schedule C for sole proprietors).
- Make quarterly estimated tax payments if you expect to owe \$1,000 or more in taxes.
- Pay self-employment tax if your net earnings are \$400 or more.
- File employment tax returns if you have employees (Forms 941/944, W-2, W-3, 940, etc.).
- File information returns such as 1099-NEC for payments to independent contractors.

Record Keeping

- Keep records of all income and expenses.
- Retain supporting documents such as receipts, invoices, contracts, and mileage logs.
- Maintain records for at least 3 years (4 years for employment tax records).

Common Small Business Deductions

- **Advertising and Marketing:** Website costs, business cards, online ads, print/radio/TV ads.
- **Car and Truck Expenses:** Standard mileage rate (70¢/mile for 2025) or actual expenses (gas, repairs, insurance, depreciation, etc.), plus parking fees and tolls for business use.
- **Contract Labor:** Payments to independent contractors (report on 1099-NEC if \$600 or more).
- **Depreciation and Section 179 Deduction:** Deduct the cost of business equipment, furniture, computers, and certain vehicles over time or expense up to \$1,250,000 in 2025 (subject to phase-out).
- **Employee Wages and Benefits:** Salaries, bonuses, employer-paid health insurance, retirement plan contributions, and certain fringe benefits.

Common Small Business Deductions Cont'd

- **Insurance:** Business insurance (liability, property, malpractice, workers' comp, etc.), and health insurance for self-employed individuals (deductible on Schedule 1).
- **Interest:** Interest on business loans, credit lines, and business credit cards (allocate between business and personal use as needed).
- **Legal and Professional Fees:** Fees paid to accountants, attorneys, consultants, and tax preparers (business portion only).
- **Office Expenses:** Office supplies, postage, software, and small equipment.
- **Rent or Lease Payments:** Rent for office, storefront, equipment, or vehicles (not if you have or will receive equity in the property).
- **Repairs and Maintenance:** Repairs to business property and equipment (not improvements).
- **Supplies:** Items used in the course of business (not inventory).
- **Taxes and Licenses:** State and local business taxes, real estate taxes on business property, personal property taxes, business licenses, and regulatory fees.
- **Travel, Meals, and Entertainment:** Airfare, hotels, car rental, business mileage, and 50% of business-related meals (entertainment is generally not deductible).
- **Utilities:** Electricity, water, gas, trash, telephone (business portion only).
- **Other Expenses:** Bank fees, education expenses, dues to business organizations, impairment-related expenses, moving machinery, outplacement services, penalties for late performance of a contract, etc.

Deductions to Watch Out For (Often Missed or Special Rules Apply)

- **Business Use of Home (Home Office Deduction):** If you use part of your home exclusively and regularly for business, you may deduct a portion of mortgage interest, rent, utilities, insurance, repairs, and depreciation, or use the simplified method (\$5 per square foot, up to 300 sq. ft.).
- **Startup and Organizational Costs:** You can deduct up to \$5,000 of startup costs and \$5,000 of organizational costs in the first year (reduced if costs exceed \$50,000), with the remainder amortized over 15 years.
- **De Minimis Safe Harbor for Tangible Property:** You may deduct up to \$2,500 per item or invoice for tangible property purchases (or \$5,000 if you have an applicable financial statement).
- **Bad Debts:** Deductible if previously included in income and become uncollectible (accrual method only).
- **Qualified Retirement Plan Contributions:** SEP, SIMPLE, or qualified plan contributions for yourself and employees.
- **Qualified Business Income Deduction (QBI):** Up to 20% deduction for qualified business income (see Form 8995/8995-A).
- **Charitable Contributions:** Not deductible on Schedule C, but may be deductible on Schedule A if you itemize.

Deductions Not Allowed

- Personal, living, or family expenses
- Political contributions, lobbying expenses
- Penalties and fines for breaking the law
- Club dues (athletic, social, etc.)
- Entertainment expenses (with limited exceptions)
- Capital improvements (must be depreciated)
- Charitable contributions (on Schedule C)
- Settlements or payments related to sexual harassment or abuse if subject to a nondisclosure agreement

Other Key Tips

- Always separate business and personal expenses.
- Keep detailed records and receipts for all deductions.
- Review IRS Publications 334, 463, 535, 587, and 583 for more details.