Small Business Tax Credits And Deductions

As a small business owner, every dollar counts. Understanding the right tax credits and deductions can make a significant difference in your bottom line, enabling you to reinvest in growth and drive your business forward. But to truly maximize these opportunities, you need to stay proactive and well-informed.

While the available credits and deductions are specific to each business, we'll review some that apply to a wide range of businesses.

Deductions: reduce your taxable income

The IRS allows businesses to reduce their taxable income by deducting expenses that are both ordinary and necessary - meaning they should be common in your industry and helpful for your business. Here's a look at some key deductions:

Startup costs

You can deduct up to $5,000 in startup costs in your first year of business, provided your total startup costs are less than $50,000. If your costs exceed $50,000, your available first-year deductions will be reduced dollar for dollar. Any start-up costs that are not deductible in the first year are amortized over 180 months.

Home office deduction

If you use part of your home exclusively as your primary place of business, you may qualify for the home office deduction. You can calculate it using the simplified method, which permits a maximum deduction of $1,500 based on the square footage of your office. Or, you can use the regular method, which allows for a deduction based on actual expenses. This method can lead to a larger deduction but requires more detailed records.

Vehicle expenses

You can deduct the cost of using your vehicle for business by either claiming the standard mileage rate or deducting actual vehicle expenses such as gas and maintenance. This deduction is available any time you incur vehicle expenses for business purposes, regardless of how often you use the vehicle for work.

Please note that you may also be able to depreciate all or a portion of the cost of a vehicle if it's used at least 50% of the time for your business.

Business meals

50% of business-related meal expenses are deductible as long as they are directly related to business activities.

Travel expenses

Expenses for airfare, lodging, meals, and other costs incurred during business travel are deductible if the primary purpose of the trip is business-related.

Employee wages and benefits

Salaries, wages, and employee benefits, such as health insurance, are deductible as business expenses.

Professional fees

Fees paid to accountants, attorneys, or consultants for business-related activities are fully deductible.

Bad debts

If you loan money and aren't repaid, you may be able to deduct the uncollected amount as a short-term capital loss. If you sell goods on credit and report your income on an accrual basis and aren't paid, you may be able to deduct the uncollected amount as a bad debt.

Qualified Business Income

The Qualified Business Income or QBI deduction allows pass-through entities to deduct up to 20% of their qualified business income. However, certain service businesses, like law firms and accounting firms, may face limitations on this deduction if the owner's income exceeds a specific threshold.

For 2024, the full deduction is available to individuals with taxable income up to $191,950 or $383,900 for married couples. If your income exceeds these amounts, the deduction might be limited or phased out entirely. Keep in mind that the QBI deduction is set to sunset after 2025 unless new legislation extends it.

When it comes to maximizing tax savings with a pass-through entity, there's a bit of strategy involved. Owners of these entities generally want to keep their regular compensation or wages as low as possible while maintaining a reasonable salary, which is necessary to avoid raising red flags with the IRS. By doing so, you can maximize pass-through distributions, which are taxed more favorably than wages, and qualify for the QBI deduction.

Depreciation

If you purchase business assets like machinery, vehicles, or office equipment, you can depreciate them over time. This allows you to deduct a portion of the asset's cost each year.

Section 179

The Section 179 deduction allows businesses to deduct the full purchase price of qualifying equipment and software the year they're placed in service rather than spreading the deduction over several years through depreciation. Almost any depreciable property used at least 50% of the time for business purposes can qualify for the deduction.

For 2024, the maximum deduction is $1.22 million, but the deduction begins to phase out dollar for dollar once total asset purchases exceed $3.05 million. Also, this deduction cannot be used to create or increase a net operating loss.

Bonus Depreciation

Bonus Depreciation is another option for deducting a large percentage of the cost of eligible assets upfront. It applies to new and used property as long as it's used for business and has a depreciable life of 20 years or less. Unlike Section 179, Bonus Depreciation does not phase out. It can be used to create a net operating loss and can also be carried forward.

In 2024, bonus depreciation allows for a 60% deduction of the cost of eligible assets, but this deduction will decrease by 20% annually until it phases out in 2027.

Tax credits

After applying all relevant deductions, you'll arrive at your taxable income. This is where tax credits come into play, directly reducing your tax liability. Here are some key tax credits available to small businesses:

Work Opportunity Tax Credit

The Work Opportunity Tax Credit incentivizes businesses to hire individuals from certain groups facing barriers to employment. These groups include veterans, individuals with disabilities, the formerly incarcerated, and those experiencing long-term unemployment, among others.

The Credit is available to businesses of all sizes for employees who begin work on or before December 31, 2025. A maximum credit of $2,400 is available for each qualified employee, depending on total wages and hours worked.

Small Business Health Care Tax Credit

The Small Business Health Care Tax Credit can cover up to 50% of the premiums paid for employees' health insurance.

To qualify, your business must have fewer than 25 full-time employees with average annual wages below $56,000. Additionally, you must cover at least 50% of the health insurance premiums for your employees, not including dependents, and the plan must be purchased through the Small Business Health Options Program.

Retirement Plans Startup Costs Tax Credit

Setting up a retirement plan, like a 401(k) or SIMPLE IRA, can boost employee morale but also comes with added costs. Fortunately, the IRS offers a tax credit to small businesses to offset the costs of establishing a new plan, covering up to $5,000 per year for the plan's first three years.

To qualify, you must have 100 or fewer employees earning at least $5,000 annually, and at least one plan participant must be a non-highly compensated employee. For businesses with 50 or fewer employees, the Credit can be up to 100% of eligible startup costs. Businesses with 51 to 100 employees can claim up to 50% of startup costs. Please note that you can't deduct the startup costs and simultaneously claim the tax credit for the same expenses.

Disabled Access Credit

The Disabled Access Credit provides up to $5,000 annually for small businesses that incur expenses to make their facilities accessible to individuals with disabilities. To qualify, your business must have earned $1 million or less or had 30 or fewer full-time employees in the previous year.

Next Step

Tax deductions and credits are highly specific to your business. While we've highlighted a few that may apply, this list is not exhaustive and doesn't replace personalized advice. A skilled accountant can help you identify every possible credit and deduction available to your business. Contact our office today, and we'll ensure you're maximizing your tax savings and making the most of every opportunity.

About Heard, McElroy & Vestal

In 1946, S. Berton Heard, Charles McElroy and Charles Vestal founded Heard, McElroy & Vestal, LLC in Shreveport, Louisiana. Together, this trio of professionals established the firm as a pillar of trust, integrity and competence, with the mission to create solutions and provide opportunities for our clients, our people, and our communities. HMV is one of the largest public accounting and consulting firms in Northwest Louisiana, servicing our clients throughout the states of Louisiana, Arkansas, Texas, Mississippi, Oklahoma and Tennessee from offices in Shreveport and Monroe. Our firm is comprised of over one hundred (100) employees: Partners, Of Counsel Partners, Senior Managers, Managers, additional Professional Staff and Administrative Staff. Our Professional Staff includes more than fifty (50) certified public accountants who obtain additional certifications which are Accredited in Business Valuation (ABV), Certified Fraud Examiners (CFE), Not-for-Profit Certificate holders, Certified Valuation Analysts (CVA), Personal Financial Specialists (PFS), and Certified Mineral Managers (CMM). Our team of professionals brings together many years and diversification of experience, providing a network of knowledge and resources and allowing for industry and niche specialization. Not one CPA can offer the range and quality of services a firm of our size is able to provide, while remaining small enough to deliver personalized service and attention to our clients with consistency on engagements. HMV's strategic associations include Aliign Mineral Management, LLC, Business Valuation Consultants, LLC and HMV Wealth Advisors, LLC.

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