PacificCPE

COURSE
34504A

Small Business Tax: Income, Gross Profit, and Credits

Understanding what counts as business income—and how to account for it properly—is essential for accurate small business returns. This course covers the general business credit, walks through the various categories of business income, explains what items are excluded from income, and addresses cost of goods sold calculations using Schedule C. It wraps up with an overview of figuring gross profit, giving practitioners a complete picture of the income side of the return.

CREDIT HOURS 2 | FIELD OF STUDY TAXES | EXAM QUESTIONS 10

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Assignment

- Study the full course materials included here.
- Complete the review questions after each chapter.
- Answer 10 final exam questions.
- Final exam is scored immediately, 70% or better passes.
- Certificate of completion is available in your account.
- Failed exams can be retaken free of charge.

Course Objectives

- Recall various common business tax credits.
- Identify the proper treatment for various forms of business income.
- Recall the factors of calculating cost of goods sold.
- Recognize how to calculate gross profits.

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Chapter 1: GENERAL BUSINESS CREDIT

Chapter Objective

After completing this chapter, you should be able to:

- Recall various common business tax credits.

I. OVERVIEW

A business's general business credit for the year consists of the carry-forward of business credits from prior years plus the total of the current year business credits. In addition, a business's general business credit for the current year may be increased later by the carry-back of business credits from later years. This credit is subtracted directly from a business's tax liability.

All of the following credits are part of the general business credit. The form used to figure each credit is shown in parentheses. Form 3800 will also have to be completed.

A. MISCELLANEOUS CREDITS

The following are some of the miscellaneous credits available for the 2026 tax year.

1. Credit for Employer Social Security and Medicare Taxes Paid on Certain Employee Tips (Form 8846)

The credit is generally equal to a business's (employer's) portion of social security and Medicare taxes paid on tips received by employees of a food and beverage establishment where tipping is customary.

The credit applies regardless of whether the food is consumed on or off the business premises.

However, the business cannot get credit for its part of social security and Medicare taxes on those tips that are used to meet the federal minimum wage rate that applies to the employee under the Fair Labor Standards Act.

2. Credit for Employer-Provided Childcare Facilities and Services (Form 8882)

Effective January 1, 2026, the employer-provided child care tax credit (Section 45F) equals 40% of qualified child care expenditures (up from 25% prior to 2026). Eligible small businesses can claim up to 50%. The credit also covers 10% of qualified resource

and referral expenditures, with a maximum annual credit of $500,000 ($600,000 for small businesses).

3. Low-Income Housing Credit (Form 8586)

This credit generally applies to qualified low-income housing buildings placed in service after 1986. For more information, see Form 8586.

4. Orphan Drug Credit (Form 8820)

Use Form 8820 to figure and claim the orphan drug credit and to elect the reduced credit under section 280C. The credit is 25% of qualified clinical testing expenses paid or incurred during the tax year.

5. Credit for Small Employer Pension Plan Startup Costs, Contributions, Auto-Enrollment, and Military Spouse Participation (Form 8881)

Eligible small employers use Form 8881 to claim the credit for qualified startup costs incurred in establishing or administering an eligible employer plan. For an eligible small employer, the credit is 50% of the qualified startup costs paid or incurred during the tax year. The credit is limited to the greater of $500 or the lesser of $250 for each employee that is eligible to participate in the plan or $5,000 for the first tax year and each of the following 2 tax years. No credit is allowed for any other tax year.

6. Credit for Small Employer Health Insurance Premiums (Form 8941)

This is available to eligible small employers, generally those with 25 full-time equivalent employees (FTEs) or less. The maximum credit is a percentage of premiums the employer paid during the tax year for certain health insurance coverage the employer provided to certain employees enrolled in a qualified health plan offered through a Small Business Health Options Program (SHOP) Marketplace. For tax years beginning after 2013, the credit is only available for a 2 consecutive tax year credit period. The credit may be reduced by limitations based on the employer's full-time equivalent employees, average annual wages, adjusted average premiums, and state premium subsidies and tax credits. For more information, see Form 8941.

B. WORK OPPORTUNITY CREDIT (FORM 5884)

1. Purpose of Credit

The work opportunity credit can be claimed for qualified first- and/or second-year wages paid to or incurred for targeted group employees during the tax year. A business does not have to be located in an empowerment zone or rural renewal county to qualify for this credit.

A business can claim or elect not to claim the work opportunity credit any time within 3 years from the due date of your return on either your original return or an amended return.

Partnerships, S corporations, cooperatives, estates, and trusts must file Form 5884 to claim the credit. All other taxpayers are not required to complete or file this form if their only source for this credit is a partnership, S corporation, cooperative, estate, or trust. Instead, they can report this credit directly on Form 3800, General Business Credit.

2. Members of Targeted Groups

A job applicant may be certified as a member of a targeted group if he or she is described in one of the following groups.

Qualified IV-A Recipient An individual who is a member of a family receiving assistance under a state plan approved under part A of title IV of the Social Security Act relating to Temporary Assistance for Needy Families (TANF). The assistance must be received for any 9 months during the 18-month period ending on the hiring date.

Qualified Veteran A veteran who is any of the following:

- A member of a family that has received Supplemental Nutrition Assistance Program (SNAP) benefits (food stamps) for at least a 3-month period during the 15-month period ending on the hiring date.
- Unemployed for a period or periods totaling at least 4 weeks (whether or not consecutive) but less than 6 months in the 1-year period ending on the hiring date.
- Unemployed for a period or periods totaling at least 6 months (whether or not consecutive) in the 1-year period ending on the hiring date.
- A disabled veteran entitled to compensation for a service-connected disability and is hired not more than 1 year after being discharged or released from active duty in the U.S. Armed Forces.
- A disabled veteran entitled to compensation for a service-connected disability and was unemployed for a period or periods totaling at least 6 months (whether or not consecutive) in the 1-year period ending on the hiring date.

Note

Requesting the information in box 4 or box 5 of Form 8850 is an exception to the Americans with Disabilities Act's prohibition on pre-offer disability-related inquiries. The purpose of this request is to support the hiring of certain disabled veterans, which will entitle the employer to a larger work opportunity credit than the hiring of other targeted group members.

To be considered a veteran, the applicant must:

- Have served on active duty (not including training) in the Armed Forces of the United States for more than 180 days or have been discharged or released from active duty for a service-connected disability, and
- Not have a period of active duty (not including training) of more than 90 days that ended during the 60-day period ending on the hiring date.

Qualified Ex-Felon

An ex-felon who has been convicted of a felony under any federal or state law, and is hired not more than 1 year after the conviction or release from prison for that felony.

Designated Community Resident

An individual who is at least age 18 but not yet age 40 on the hiring date and lives within an empowerment zone, an enterprise community, or a renewal community and continues to reside at the locations after employment.

Vocational Rehabilitation Referral

An individual who has a physical or mental disability resulting in a substantial handicap to employment and who was referred to the employer upon completion of (or while receiving) rehabilitation services by a rehabilitation agency approved by the state, an employment network under the Ticket to Work program, or the Department of Veterans Affairs.

Summer Youth Employee

An individual who:

- Performs services for the employer between May 1 and September 15,
- Is at least age 16 but not yet age 18 on the hiring date (or if later, on May 1), and

- Lives within an empowerment zone, enterprise community, or renewal community.

SNAP Benefits (Food Stamps) Recipient

An individual who:

- Is at least age 18 but not yet age 40 on the hiring date, and
- Is a member of a family that:
  - Has received SNAP benefits for the 6-month period ending on the hiring date, or ▫ The family received SNAP benefits for at least 3 months of the 5-month period ending on the hiring date.

SSI Recipient

An individual who is receiving supplemental security income benefits under title XVI of the Social Security Act (including benefits of the type described in section 1616 of the Social Security Act or section 212 of Public Law 93-66) for any month ending during the 60-day period ending on the hiring date.

Long-term Family Assistance Recipient

An individual who is a member of a family that:

- Has received TANF payments for at least 18 consecutive months ending on the hiring date, or
- Receives TANF payments for any 18 months (whether or not consecutive) beginning after August 5, 1997, and the earliest 18-month period beginning after August 5, 1997, ended during the past 2 years, or
- Stopped being eligible for TANF payments because federal or state law limits the maximum period such assistance is payable and the individual is hired not more than 2 years after such eligibility ended.

Qualified Long-term Unemployment Recipient

An individual who has been unemployed for not less than 27 consecutive weeks at the time of hiring and received unemployment compensation during some or all of the unemployment period.

3. Qualified Wages

Wages qualifying for the credit generally have the same meaning as wages subject to the Federal Unemployment Tax Act (FUTA). If the work performed by any employee during more than half of any pay period qualifies under FUTA as agricultural labor, that employee’s wages subject to social security and Medicare taxes are qualified

wages. For a special rule that applies to railroad employees, see section 51(h)(1)(B). Qualified wages for any employee must be reduced by the amount of any work supplementation payments the employer received under the Social Security Act for the employee.

The amount of qualified wages for any employee is zero if:

- The employee did not work for at least 120 hours,
- The employee worked for the employer previously,
- The employee is the employer's dependent,
- The employee is related to the employer (see section 51(i)(1)), or
- 50% or less of the wages the employee received from the employer were for working in the employer's trade or business.

Qualified wages do not include:

- Wages paid to or incurred for any employee during any period for which the business received payment for the employee from a federally funded on-the-job training program;
- Wages paid to or incurred for a summer youth employee for services performed while the employee lived outside an empowerment zone;
- Wages paid to or incurred for a designated community resident for services performed while the employee lived outside an empowerment zone or rural renewal county;
- Wages paid to or incurred for services performed by a summer youth employee before or after any 90-day period between May 1 and September 15;
- Wages for services of replacement workers during a strike or lockout;

4. How to Claim the Credit

Abusiness must request and be issued a certification for each employee from the state workforce agency (SWA). The certification proves that the employee is a member of a targeted group. The business must either:

- Receive the certification by the day the individual begins work, or
- Complete Form 8850, Pre-Screening Notice and Certification Request for the Work Opportunity Credit, on or before the day the business offers the individual a job and receives the certification before it claims the credit.