

INCOME**EARNED****SELF-EMPLOYMENT OR SMALL BUSINESS INCOME**

Description: Self-employment, small business or farm income is income that results from work activity on the part of the A/R, in which s/he is self-directing and receives compensation directly from the customer.

Policy: After allowable business expenses have been deducted, the remaining income is considered available earned income of the A/R and is subject to the appropriate budgeting methodology based on the category of the A/R.

References: SSL Sect. 366.2(b)
Dept. Reg. 360-4.3(c)
GIS 09 MA/025
01 MA/024

Interpretation: When an individual is self-employed or owns or operates a small business in which s/he is employed, certain costs related to the business or self-employment (e.g. the cost of materials, supplies, and labor) are deducted from the gross income for the purpose of determining eligibility for Medicaid.

Following are some of the items of business expenditures which are generally deductible from gross business income:

- Rental of quarters, equipment, or furniture;
- Salaries and fringe benefits of employees;
- Cost of goods for re-sale;
- Business taxes, licenses and permits;
- Cost of tools, supplies and raw materials;
- Insurance for the business;
- Lights, heat, water, sewage and telephone charges;
- Advertising and travel;
- Taxes and carrying charges on any property used in the business.

NOTE: For SSI-related A/Rs, depreciation costs for buildings, equipment and materials necessary for and directly related to the operation of the business are also deducted from gross income. Depletion, amortization and 179 expenses, which are types of depreciation, may also be deducted for the SSI-related.

INCOME

SELF-EMPLOYMENT OR SMALL BUSINESS INCOME

Following are some of the items of business expenditures, which are **not** deductible from gross business income:

- Payments on the principal for real property used wholly or partially in the business;
- Any expenses which are not directly related to the operation of the business, (for example, personal expenses such as lunch or transportation for work).

Income and expenses are generally considered on an annual basis. The difference between income and expenses is then divided by 12 to establish the A/R's monthly earned income. One possible source for verifying the A/R's income and expenses is his/her income tax records.

How to Estimate Net Earnings from Self-Employment:

If the A/R has been conducting the same trade or business/farm for several years; has had net earnings which have been fairly constant from year to year; and anticipates no change or gives no satisfactory explanation why net earnings would be substantially lower than in the past, take the net profit from the past year as an estimate for the current year. Divide yearly net profit by 12 to determine monthly income.

If an A/R is engaged in a new trade or business/farm, obtain the A/R's profit and loss statement or other business records for previous three months, or give the A/R the Financial Status (Farm or Business) Form (DOH-4469) to complete. Divide net profit, by 3 to project monthly income for the next three months. If an A/R is engaged in a business which is seasonal or has unusual income peaks, eligibility may need to be redetermined more frequently than annually if changes are reported by the A/R. Seasonal income is only applied for the seasonal time period.

NOTE: When using the three-month business record, a loss in one month may be used to offset a profit in another month.

INCOME

SELF-EMPLOYMENT OR SMALL BUSINESS INCOME

Procedure to Determine Net Profit

Income Tax Return

<u>Business Organization</u>	<u>Documentation</u>
Single Owner Business/Farm	tax return including Schedule C or C-EZ or Schedule F (farm) or accountant's statement or business records/ledgers or signed statement from owner (e.g., financial status form)
Partnership	tax return including Schedule E or F (farm) or Form 1065 and Schedule K-1 and W-2 if applicable or accountant's statement or partnership agreement or Form 1065, Partnership Return or Schedule K-1 (1065) or statement from partners and business records or ledgers or signed statement from owner (e.g., financial status form)
S-corporation	tax return (Form 1120S) Schedule K-1 W-2 if applicable

Take net profit from appropriate lines of schedules, and:

For LIF, Medically Needy (ADC-Related) and S/CC A/Rs, add back any depreciation, depletion, amortization or 179 expenses, deducted; **or**

For SSI-related A/Rs, because depreciation, depletion, amortization, 179 expenses are allowed, use net profit as gross income.

NOTE: One-half of self-employment tax as listed under Adjustments to Income on Form 1040, is an allowable deduction for all categories.

Accountant's Statement, Business Records, Financial Statement Form from A/R:

Take gross receipts or sales and deduct business expenses.

INCOME

SELF-EMPLOYMENT OR SMALL BUSINESS INCOME

Do not allow personal expenses and entertainment, personal transportation, purchase of capital equipment to expand a business*, or payment on the principal of loans or mortgages. Depreciation, depletion, amortization and 179 expenses may be allowed for SSI-related A/Rs.

***NOTE:** The repair or replacement of existing capital equipment is allowed.

Assume that all deductions taken on tax returns or business records are allowed by the IRS, unless there is evidence to the contrary.

If tax returns or **annualized** business records indicate a loss (negative dollar amount), use zero income.

EXCEPTION: Within a single type of business, use zero income only when the tax return or business record indicates a cumulative loss, for example: an A/R has three rental properties; two show a net profit and one shows a net loss; use the loss to off-set the profits, and do not reduce the loss to zero unless the cumulative bottom line for the three properties is a negative dollar amount.

If tax returns, accountant's statement, or business records are not available:

- obtain written statement from the A/R;
- ask for any documentation verifying income/expenses;
- have A/R keep business records for future determination of net profit.

DOH-4469 Financial Status (Farm or Business) form can be used in the following situations to establish a three month financial snapshot of a business:

- When the A/R indicates that the business is new, and no federal tax return has yet been filed;
- When the A/R indicates that last year's tax return is not representative of the current year's earnings;
- When the A/R indicates that s/he does not file a tax return for the business.

INCOME

SELF-EMPLOYMENT OR SMALL BUSINESS INCOME

Inasmuch as, the DOH-4469 reflects a three month financial snapshot of a business, it is appropriate to allow a loss in one month to offset a profit in another month. When using an annualized business record such as a tax return or an accountant's statement, a business loss is brought to zero, and cannot be used to reduce income from another source.

A/Rs are not required to supply actual bills and receipts to substantiate the income and expenses recorded on the Financial Status form (DOH-4469). The applicant's certification on the bottom of the form, that the information is true and correct, is sufficient.

How to Verify Status: In verifying income from self-employment or small business/farm it is essential to determine what kind of operating costs are necessary and how the income is obtained. Such factors as accounts payable and receivable, inventory levels and investments which are expected to yield long term dividends, need to be evaluated.

Documentation: Sufficient to establish an audit trail.

Since business records are often quite complex, the preferable method of documentation is by photocopy. If this is impossible, all documents used in arriving at the determination are listed as in the following example which pertains to a service station operator:

Receipted bill from Excelsior Oil Co. dated 8/15/83 seen.
Paid \$500 for 500 gallons of gasoline at \$1.00 per gallon.

Disposition: When the gross business income is determined and the business expenses are determined and deducted, the resulting amount is earned income.

NOTE: The A/R's income is evaluated against the maintenance picture of the A/R. (See **OTHER ELIGIBILITY REQUIREMENTS FINANCIAL MAINTENANCE**)