SNAP 503-1
INCOME
Self-Employment Income

Supersedes: SNAP 503-1 (08/03/2022)

Reference: 7 CFR 273.10 and 7 CFR 273.11; ARM 2.4.113

Overview: Net earnings from self-employment must be counted when determining eligibility for the Supplemental Nutrition Assistance Program (SNAP).

DEFINITION OF SELF-EMPLOYMENT:

Self-employment is the act of engaging in a trade or business. A trade or business is generally an activity carried on for a livelihood or in good faith to make a profit. An individual does not have to make a profit to be in a trade or business as long as a profit motive exists. The individual may be a contractor, franchise holder, owner/operator, partner, etc. The individual must meet the following criteria to be considered self-employed:

1. They earn their income directly from their business or trade not from wages or salary from an employer.
2. They are responsible for the payment of their entire Social Security and Federal withholding taxes.
3. They do not have an employee/employer relationship with another individual, and the services performed cannot be controlled by an employer such as setting the job schedule, etc.; and,
4. They sometimes file self-employment tax forms (Schedule F, C, C-EZ, SE, Form 1065, etc.).

NOTE- LLCs and S-Corporations are not considered Self-Employment.

SELF-EMPLOYMENT STRUCTURES:

There are many types of self-employment structures. Eligibility staff should determine the structure based on how the income flows to and from the household member, rather than applying rules based on how the business is classified.

Unincorporated v. incorporated is the first important distinction. Again, even a business with a name ending in “Inc.” might not actually be incorporated, and some incorporated businesses might not use “Inc.” in their name. Eligibility staff determine the correct structure during the interview.

These guidelines apply when determining whether a business is **self-employment**:

- The income and resources of an **unincorporated** business, whether a sole proprietorship or a partnership, are treated as **self-employment income** and resources of the owner(s).

- Income earned as an employee of an **incorporated business** (typically a corporation) is treated as **earned income**, and the value of stocks or dividends someone held as a shareholder is treated as a resource. Wages paid to corporate officers or employees are considered wages, but fees paid to corporate officers are considered self-employment earnings. Any corporate income reported on Schedule E as income received from a corporation must be annualized and used as <u>countable unearned</u> income even if the household did not receive the money. Any loss reported on Schedule E as loss received from a corporation is not used in any budget calculation.

SELF-EMPLOYMENT STRUCTURES

These structures **ARE** self-employment and income and costs of producing income are entered as self-employment in CHIMES:

1. **<u>Sole Proprietorship</u>**: A self-employment business that is not incorporated and has one owner. The business income and liabilities are the responsibility of a single owner.
2. **<u>Partnership:</u>** A self-employment business set up with two or more partners. In addition to personal income tax forms, partnerships are also required to file 1065 and K-1 forms. The business income and liabilities are the responsibility of all the partners with the partnership defining shares of ownership and responsibility. Partnership income is determined in the same way as other self-employment.
3. **<u>Independent Contractor:</u>** An individual who pays their own employment taxes and does not have an employee/employer relationship is considered self-employed.
4. **<u>Sharecropper:</u>** If the sharecropper pays the costs of doing business and receives a portion of the net income in exchange for labor, the sharecropper is considered self-employed. The sharecropper is not considered self-employed if the sharecropper is not responsible for paying the costs of doing business.

********** STRUCTURES <u>NOT CONSIDERED</u> TO BE SELF-EMPLOYMENT*************

1. <u>LLC-LIMITED LIABILITY COMPANY</u>
2. <u>S-CORPORATIONS</u>
3. <u>CORPORATIONS</u>

For SNAP purposes, owners of LLCs, S-Corporations, and any other corporations are considered employees of the corporation and therefore, cannot be considered self-employed. Because these SNAP participants are not considered self-employed, **they are not entitled to the exclusion of allowable costs of producing self-employment income. The income from these types of corporations should be treated as regular earned income (wages and salaries), not self-employment income.** Corporations are legal entities and are responsible for their own debts and obligations. We must determine the correct type of business structure during the interview (SEE: Corporations, S-Corps, and LLC Income Business Process).

An S-Corporation must file an annual information return (IRS Form1120 and 1120 K-1) to report the income, deductions, gains, losses, distributions, etc., from its operations, but it does not pay income tax. Profits or losses are "passed through" to its shareholders.

Each shareholder includes his or her share of the partnership's income or loss on his or her tax return (IRS 1040). The 1040 form will outline the SNAP participant's income (to be entered as wages & salaries).

Although these corporations are not considered self-employment, the income from these corporations, as reported on the household's Form 1040, should be counted in determining the household's eligibility and benefit level. The income would then be annualized. If the corporation has not filed taxes yet (i.e., a new business), the worker would anticipate income until a tax form is available. Distributions and other payments by an LLC, S-Corporation, or a corporation to a corporate officer must be treated as wages if it is listed on the individual's 1040. If distributions are found on the Schedule K for the corporation but are not found on the individual's 1040; we would want to clarify whether those distributions were reinvested into the company.

- Fees paid to corporate officers **<u>are considered wages and salaries</u>** – they are paid to corporate officers in exchange for work performed but taxes are not withheld. This income will usually be reported on the INDIVIDUAL'S 1040 form.
- The value of stocks or dividends someone held as a shareholder is treated as a resource. Resources are not considered for CE and ECE households.
- In certain situations, a client might submit a Schedule C and a 1040. This usually happens when an owner of an LLC did not pay themselves *wages* but took disbursements/dividends of the business' profit. This income can be located on line 3 of the 1040 and should be annualized. It is important during the interview to determine how the applicant is paying themselves.

<u>EARNED VS. UNEARNED</u>:

Self-employment income is considered **earned income** (entered in CHIMES as Self-Employment). The income is considered **unearned income if any of the following occur**:

1. Rental income and rental partnership income, and the individual is not actively participating in the business at least 20 hours per week (SNAP 501-1);
2. Contract for deed income (SNAP 501-1); or
3. In some instances, boarder income (SNAP 201-4).

RESOURCES:

Property essential to self-employment is excluded as a resource. Possible exclusions of some resources are:

1. Property Essential for Self-employment (SNAP 402-1).
2. Income Producing Property (SNAP 402-1); and,
3. Business Checking Accounts (SNAP 402-1).
   NOTE: Money in a business checking account is a countable resource, but the self-employment funds prorated as income are excluded as a resource. The self-employment funds prorated as income retain their exclusion for the time they are prorated as income even if the funds are commingled.

INCOME EXCLUSIONS:

The following are income exclusions:

1. Federal gasoline tax credit.
2. State gas tax.
3. Disaster payments (SNAP 501-1).
4. Crop insurance payments; and,
   NOTE: If a Federal Insurance Corporation Payment or a private insurance payment is paid in a lump sum, it is excluded as income and counted as a resource. If the payment is from a private insurance company and pays the household in installments, it is countable unearned income.
5. Patronage dividends paid to a self-employment enterprise. Patronage dividends, paid by cooperatives in cash, are countable unearned self-employment income (SNAP 501-1). If the patronage dividends are paid in stock, they are counted as a resource (SNAP 402-1).

AGRICULTURAL STABILIZATION & CONSERVATION SERVICES (ASCS):

Cash payments are counted as earned self-employment income. These include but are not limited to: Commodity Credit Corporation, acreage reduction and conservation payments, and other one-time or installment payments made to farmers for crop or other losses unrelated to a presidentially declared disaster. If the payment is due to a presidentially declared disaster, it is excluded as both income and a resource due to the Disaster Relief Act.

CANCELED DEBT:

If canceled debt appears on any of the tax forms**, it should not be counted**. Before disregarding canceled debt claimed by a household, the household is required to provide a statement from the lending institution verifying the canceled debt.

CAPITAL GAINS or CAPITAL LOSSES:

Capital gains are increases in the value of property between the time purchased and the time sold. Capital losses are decreases in the value of property between the time purchased and the time sold. Depreciation is considered when determining whether capital gains/losses occur for self-employment businesses. Capital gains/losses are usually determined at the time property is sold. Capital gains from the sale of self-employment property must be annualized as part of the net earnings from self-employment whether paid in a lump sum or in installments. Capital gains are included in prospectively budgeting self-employment income if capital gains are received or are expecting to be received prospectively for next year.

Capital losses are not used in any self-employment income determination. They are not considered business expenses or deductions.

ALLOWABLE EXPENSES OF PRODUCING SELF-EMPLOYMENT INCOME:

Allowable expenses of producing self-employment income are deducted from the gross self-employment income. Most costs of doing business are allowable expenses **and may be accepted as listed on the income tax forms or other documentation with few exceptions.** Self-employment income for SNAP purposes is not computed the same as it is for Internal Revenue Service (IRS) purposes. The IRS forms may only be used for verification purposes. Expenses must be current, not due from a previous fiscal period, and are allowed when they are billed or otherwise become due. **NOTE:** Some self-employed individuals do not claim all expenses on their Schedule C in order to qualify for Earned Income Tax Credit. The allowable expenses not shown on the Schedule C can be verified by the household and used in determining accurate self-employment earnings. Allowable costs of producing self-employment income include, but are not limited to:

1. Payments on the principal of the purchase price of income producing real estate and capital assets, equipment, machinery, and other durable goods even if the capital asset or durable good is not set up on a depreciation schedule. Capital assets and durable goods are objects used in business expected to last a long time such as farm machinery, equipment, swing sets, buildings, computers, cribs, VCRs, DVDs, furniture, highchairs, tricycles, vehicles, hair dryers, etc.
2. Interest paid to purchase income producing property, insurance premiums, and taxes paid on income producing property.
3. Labor paid to non-household members (individuals not included in the filing unit), materials, seeds, supplies, plants and fertilizer, interest payments on business loans and operating loans, business portion of home property or expense, repairs, etc.

NOTE: Supplies include small tools, paper, pencils, scissors, oil, gas, envelopes, shampoo, hairbrushes, crayons/color books, etc. Supplies are generally described as objects usually used up or consumed in service.

NOTE: Transportation costs for doing business may be allowed; however, the cost of commuting to the business from home is not allowed. Mileage expense is allowed at the Federal business expense rate. The current rate can be found by searching for the current year standard mileage rate on the Internal Revenue Service website.

DEPENDENT CARE BUSINESS EXPENSES (Cost of meals):

Household's income from dependent care, such as a providing day care for children, elderly, or disabled individuals may elect one of the following methods to determine the **cost of meals** provided to the individuals:

1. Actual documented meals.
2. A standard per day amount based on estimated meal costs; or,
3. Current reimbursement amounts in the Child and Adult Care Food Program.

EXPENSES NOT ALLOWED FOR PRODUCING SELF-EMPLOYMENT INCOME:

Non-allowable expenses must be added back into the self-employment income if income tax forms are used or not allowed as a deduction in the monthly calculation of self-employment income. Expenses not allowable include:

1. Net losses from previous periods.
2. Personal federal, state, and local income taxes; money set aside for retirement purposes; and other work-related expenses such as transportation **to and from work**.
3. Depreciation is added back into income when used as a deduction from self-employment income.
4. Any amount that exceeds the payment a household receives from a border for lodging and meals.
5. Social Security taxes.
6. Meal and entertainment costs for the household.
7. Charitable contributions.
8. Clothing not specific to any one job; and,
9. Penalties and fines.

SELF-EMPLOYMENT CONNECTED TO HOME (E.G., FARM EXPENSES):

When a household's home is on property connected to the property used for farming or another self-employment business enterprise, the eligibility staff member must determine if the shelter costs (e.g., rent or mortgage) and the self-employment costs can be separately identified. If necessary, the eligibility staff member is required to determine a breakdown of business expenses from personal home shelter expenses by using:

1. Household's calculation of breakdown.
2. Income tax form breakdown; OR **NOTE:** If the household presents self-employment tax records (Schedule F, C, etc.); do not question the shelter deductions (utilities, insurance, interest, etc.) included on those documents.
3. Verifications submitted by the household such as: tax verifications (Ag/Nag); loan papers indicating costs of farmland, buildings, equipment, etc. versus costs for house/garage/personal equipment; insurance policy breakdowns of cost of premiums for farm and personal home costs.

If utilities are measured and billed separately, the household is entitled to the appropriate mandatory utility allowance for its residence, and to the separately billed utility costs as a self-employment cost of doing business.

If utility costs cannot be separately identified, the household is entitled to the appropriate mandatory utility allowance for its residence and does not receive a self-employment expense. **NOTE: In most instances a separate amount of utilities should be identifiable. A means of identifying costs separately is to subtract the appropriate mandatory utility allowance for the residence from the total utility costs. The remainder is allowed as a cost of doing business.**

If the household uses part of the house such as a separate room or a separate apartment solely for the self-employment business and there is a central meter, the household is entitled to the appropriate mandatory utility allowance for its residence and no deduction of utilities for the cost of doing business.

IN-HOME EXPENSE:

When the self-employment business is conducted in the household's home, and the household wants to claim a portion of its shelter expenses as a business deduction, the eligibility staff member must separate business expenses from personal shelter expenses. The portion of the home used on an exclusive basis for a business is allowed as a business expense. However, the household is not required to use the business portion as a business deduction. The household is entitled to the mandatory utility allowance for its residence and no deduction of utilities for the cost of doing business.

NOTE: If the expense is not used as a self-employment expense, it **can** be used as a shelter expense.

A substantial amount of time must be spent doing business in the home (not occasionally) to use home shelter costs as a business expense. If the in-home business **is NOT** related to dependent care, the business must also meet one of the following two conditions.

1. An allowance for space regularly used for inventory storage may be allowed if the space is identifiable and only used for self-employment; **or**,
2. The portion of the home must be used on an exclusive basis. The space allocated to the business must be used only for the business.

The eligibility staff member determines the usage of home, **with the agreement of the household,** for business purposes by:

1. The household's calculation of use.
2. Form 8829 percentage (only if the business and personal home costs are separated on this form); or,
3. The ratio of business square footage to square footage of the entire home.

The business share of home expenses is allowed as a deduction from the self-employment income as long as it is not also used as a shelter deduction. The household is not required to deduct the business share even if it can be separated from other expenses.

<u>BUDGETING AND VERIFICATION</u>

Most self-employment budgets are annualized (SNAP 601-1). Self-employment income intended to support the household on an annual basis is annualized. Temporary or seasonal self-employment income or when a business is not in operation for an entire year is income not representing annual support and is averaged over the period it is intended to cover.

The following self-employment incomes are always annualized regardless of whether the income is intended to support the household on an annual basis:

1. Farm income; and,
2. Self-employment income received less often than monthly (e.g., income received quarterly, bi-monthly, annually, etc.).

When self-employment income is annualized, the expenses must also be annualized. Expenses are counted when paid not when billed.

If the self-employment income is annualized, income tax forms (when available) should be used to determine income. The most current tax forms are used **<u>unless there is a substantial change in business or income</u>**. Income must be annualized whether tax forms reflect current income and whether they are available. Other documentation must be used to determine annualized income. Tax forms may not always be available and cannot be required of SNAP applicants. If tax forms aren’t used as verifications, eligibility staff need to request other types of verifications and determine what type of income is being received based on the definitions of earned, unearned, and self-employment income.

Other documentation examples are profit/loss statements prepared by the business, business account bank statements, or HCS 542 Self-Employment Record.

'Substantial increase or decrease in business' may include:

1. Termination or starting a new self-employment enterprise such as changing from a grain and cattle operation to a cattle operation;
2. Significant increase or reduction of operation such as adding or reducing a quarter of crop land or significantly increasing or decreasing a dairy or beef operation; and,
3. Natural disasters like hail or drought. Normal year-to-year fluctuating market prices are not considered to be substantial increases or decreases.

NEW BUSINESS:

If a new business has income, it is averaged using the income and expenses from the months the business has been in operation if the household anticipates the same for the next prospectively budgeted period. When the business has reached 12 months either at the Simplified Report or recertification, the income must be annualized if the household anticipates the same for the next prospectively budgeted period. If there is no reliable history of income or expenses to average, the eligibility staff member must negotiate a projection of the anticipated monthly income and expenses with the household.

RENTAL INCOME:

Depending on how active an individual is in managing rental property, the income is considered earned self-employment or unearned income. The cost of doing business is deducted from the gross income to determine net countable income for benefit calculation regardless of whether it is earned self-employment or unearned income.

A property owner/landlord is allowed the full amount of shelter costs (such as mortgage, taxes, insurance) that the household is required to pay to live there. The gross income minus the cost of doing business received from rental property, if a household member is not involved in management of the property 20 hours/week or more, is countable unearned income to the owner/landlord's household.
NOTE: No portion of expenses can be used as both a shelter cost and a self-employment cost.

Separate households residing in the same residence are allowed the actual amount of rent they are billed as a shelter deduction. When households reside together and **neither household owns the residence**, a rent payment made from one household to another is exempt as pass-through shelter payment up to the full amount of rent billed. If the payment is more than the full rent charged for the residence, the excess payment is unearned income to the household receiving the payment.

ROOMERS:

A roomer is an individual living with a household and paying for lodging but not meals. Refer to 'Earned vs. Unearned' in this section of the manual to determine whether the contribution is considered earned or unearned income. Payments received from roomers are usually considered unearned contributions to the household.

Do not allow expenses against the contributions unless the roomer situation meets the definition of earned income and the case is treated as self-employment.

<u>BOARDERS</u>:

Treat commercial boarding houses (businesses established as commercial enterprises offering meals and lodging for compensation with the intent to make a profit) according to the general provisions of regular self-employment rather than using the information provided below.

Boarders are individuals that a household furnishes lodging and meals (SNAP 201- 4). Foster children are not boarders. When a boarding situation is not related to a commercial boarding house, the income from boarders includes all direct payments to the household including contributions for meals and shelter. In determining the amount of countable income received from the boarder, exclude the household's costs of providing room and meals to the boarder (allowable expenses).

Households may choose one of the following methods to determine the cost of doing business (expenses):

1. The cost of the SNAP's thrifty food plan for the number of boarders in the household.
2. If the actual costs exceed the appropriate thrifty food plan, the actual documented allowable expenses of providing room and meals. If actual costs are used, only separate and identifiable costs of providing room and meals to the boarders are excluded; or,
3. A flat amount of $100 per boarder.

Expenses may not exceed the payment received by the household from the boarder. Boarder income is always earned self-employment income. Boarders may not claim separate household status to receive SNAP benefits on their own case.

<u>INCOME/LOSSES</u>:

Losses from corporations are not used to offset any other income. Farm losses are allowed only if the farm grossed or anticipated grossing at least $1,000 during the year. Farm losses may offset any other household income in the following order:

1. Other self-employment gains; and,
2. Any remainder from any other household income. If there are other wages, the 20% deduction is calculated on the gross wage prior to the farm loss being deducted.

<u>BANKRUPTCY</u>:

If bankruptcy is filed, the projected monthly self-employment income continues to be used unless the household states the business will have substantial change in income and expenses. The bankruptcy could verify this statement. **If the household reports the self-employment enterprise has ended, the monthly self-employment income is no longer prospectively budgeted**.

The self-employment income continues to count even if diverted to a bank or other source. If the self-employment income goes to a trustee and the household receives a living allowance, the entire self-employment income continues to be budgeted and no deduction is allowed for the trustee or conservator's fees. **NOTE:** The living allowance is not counted as income because the self-employment income is already being counted.

If the equipment/land is repossessed or the title is given to the lender, the property is the legal property of the lender and sale of the property is not considered income. However, if the title remains in the household's name and the lender arranges the sale, the property belongs to the household and the amount is counted as income if received as periodic payments or as a resource if received in a lump sum. If the lender forgives or writes off a loan, the amount forgiven or written off is not considered income.

Revised: December 28, 2022