



COMBINED MEDICAID 503-1 Self-Employment Income

Supersedes: FMA 503-1, (07/01/08 & 10/01/08); MA 503-1 (07/01/08)

Reference: 42 CFR 435.601; 20 CFR 416.1110(b), 416.1111(b), and 404.1065 through .1096; ARM 37.82.101

Overview: Count net self-employment income when determining Medicaid eligibility. To be considered self-employed, an individual must meet the following criteria:

1. Income is earned directly from their business/trade; they do not receive wages or salary from an employer.
2. They are responsible for full payment of their Social Security and Federal withholding taxes;
3. The individual is not employed by another person and an employer does not control or direct the services the self-employed individual performs.
4. If they file taxes, they use self-employment tax forms (schedule C, C-EZ, F, SE, Form 1065, etc.); and
5. They “materially participate” in the income production.

NOTE: Other indications of self-employment are used when a client states they are self-employed, but they haven’t yet filed income taxes. These include a business license, evidence of ongoing, regular business activities, financial accounts in the business name, periodic advertising and business registration with the Secretary of State.

SELF-EMPLOYMENT STRUCTURES:

Clients may refer to being self-employed under a variety of business structures; however, not all business structures are considered self-employment for Medicaid purposes. The most common business structures include:

1. Sole Proprietorship: Unincorporated business structure owned by one or two individuals. The owners are responsible for business income and liabilities. **NOTE:** Limited Liability Companies (LLCs) are NOT sole proprietorships.
2. Independent Contractor: Individual who pays their own employment taxes and does not have an employee/employer relationship. Considered self-employed unless incorporated or an LLC. Should be registered with Department of Labor and Industry.

3. Sharecropper: When the individual pays the cost of doing business and receives a portion of net income in exchange for their labor they are considered self-employed. However, if they are not responsible for the costs of doing business, incorporated or an LLC, they are not considered self-employed.

CORPORATIONS:

Incorporated businesses are not self-employment enterprises. Property owned by corporations and corporate stock cannot be excluded as necessary for self-employment or self-support because the individual does not own it. Even when the business started as self-employment, once it is incorporated, it is no longer considered self-employment. Income the individual receives while working for the corporation is considered countable wages. **NOTE:** Earnings paid to corporate officers are considered wages, however, fees paid to corporate directors are considered self-employment income.

ACA: Count corporate income whether or not the client receives it.

ABD and Family Medically Needy: Count any corporate income reported on Schedule E, Line 32 as unearned income only when received.

ACA: Any loss reported on Schedule E, Line 32 can be used to offset other income and decrease MAGI income.

ABD and Family Medically Needy: Losses reported on Schedule E, Line 32 are not used in any budget calculation.

LIMITED LIABILITY COMPANIES (LLC) & PARTNERSHIPS:

Medicaid treats LLCs and limited partnerships like corporations, regardless of the tax documents filed. Neither entity is considered self-employment. Guaranteed salaries are treated as regular wages; all other income received from an LLC or partnership is considered unearned income.

Property owned by an LLC or partnership cannot be excluded as necessary for self-employment or self-support because these arrangements are not considered self-employment, and the LLC/partnership owns the property, not the individual.

Partnerships are entities with two or more partners, and may include both “working” and “silent” partners. Partnerships are required to file 1065 and K-1 forms in addition to personal tax forms. All partners are responsible for business income and liabilities, with the partnership defining each partner’s share. Determine partnership income in the same manner as LLC and corporate income; income reported on a 1065 or K-1 is considered unearned, or passive income. Partnerships do not report or pay income taxes.

Only wages paid to a working partner is considered earned income, however, there won’t be a W-2 or 1099 form issued so the eligibility staff member must work with the client to determine how much, if any, of the income reported on the 1065 or K-1 is earned.

ACTIVITIES THAT ARE NOT SELF-EMPLOYMENT:

The following are treated as unearned (i.e. passive) income, and are not considered self-employment:

1. Self-employment or partnership rental income where the individual does not participate in the business at least 10 hours per week or does not report it as self-employment on Schedule C or F (passive rental income is usually reported on Schedule E). See CMA 501-1.
2. Contract for deed income (See 501-1),
3. Certain boarder income (see Boarders heading in this section), or
4. Income a “silent” (i.e., non-participating) partner receives.

RESOURCES:

ACA: Resources are not considered for any ACA program.

ABD and Family Medically Needy: See ‘Self-Employment Resources’ in CMA 402-1.

PATRONAGE DIVIDENDS:

Count patronage dividends as part of the self-employment income when paid to a self-employment business, even if paid in stock.

AGRICULTURAL STABILIZATION & CONSERVATION SERVICES (ASCS):

Count cash payments as earned self-employment income. These include, but are not limited to: Commodity Credit Corporation, acreage reduction and conservation payment and other one-time or installment payment made to farmers for crop or other losses unrelated to a presidentially declared disaster. Exclude payments due to a presidentially declared disaster as income under the Disaster Relief Act.

CANCELED DEBT:

Use canceled debt when determining net self-employment earnings, if reported on tax forms.

CAPITAL GAINS & LOSSES:

ACA: Count capital gains and subtract capital losses when determining MAGI income.

ABD and Family Medically Needy: Exclude capital gains and losses from the sale of self-employment property.

BARTERING:

Exchanging one service for another (such as storage space for appliance repair) between two self-employed businesses is called bartering. The bartered goods or services must be evaluated to determine if the value received is countable income. Food and/or shelter provided by a self-

employment business (including a farm) may be considered earned or unearned vendor/in-kind benefits.

Valuing vendor/in-kind benefits:

ABD: See 'Vendor Payments' in 501-1

Family Medically Needy: If verification is not provided, use the Family Net Monthly Income (NMI) standard for a household of one as the shelter value, and the SNAP Thrifty Food Plan for the appropriate household size for any food provided.

See 'Vendor Payment' in Sections 501-1 and 502-1 for additional information.

INCOME EXCLUSIONS:

Exclude the following when determining net self-employment income:

ACA: Disaster payments.

ABD and Family Med Needy:

1. Federal gasoline tax credit
2. State gas tax,
3. Disaster payments (see 501-1),
4. Crop insurance payments, and
5. Capital gains.

EXPENSES:

Allowable Expenses include:

1. Business transportation costs. If mileage is tracked, the Federal expense rate is used; if mileage is not tracked, allow fuel, vehicle repair and maintenance costs. **NOTE:** Only one expense method (Federal expense rate or vehicle repairs, maintenance and fuel costs) may be allowed for a vehicle for the specified period.
2. Depreciation;
3. A 7.65% deduction for the 'employer-paid' portion of Social Security taxes is allowed when determining net self-employment income. This expense is manually calculated and entered into the system.
4. Meals and entertainment costs

Other expenses allowed include: labor paid to individuals not included in the filing unit, materials, seeds, supplies, plants, fertilizer, interest payments on business loans, business portion of home property, repairs, etc. **NOTE:** Supplies are generally items that will be used up or consumed in the business, and include small tools, paper, pencils, scissors, gas, oil, envelopes, shampoo, crayons/coloring books, etc.

Deduct allowable expenses when determining net self-employment income. Most costs of doing business are allowed, and the amounts listed on the income tax forms are acceptable verification, unless the client expects their income to change. The expenses must be current and are only allowed when paid, not when incurred. **NOTE:** Expenses expected to be due and payable in the prospective period can be anticipated when calculating income for a new self-employment business or one experiencing a significant change.

To qualify for the Earned Income Tax Credit, some self-employed individuals may not claim all expenses on their Schedule C. Allowable expense not listed on the Schedule C can be verified and used to accurately determine countable self-employment earnings.

Determining Cost of Dependent Care Meals:

Self-employed dependent care providers (day care for children, elderly or disabled individuals) may choose one of the following methods to determine cost of meals provided to those they care for:

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

Shelter Expenses:

Self-Employment Business Connected to or on Home Property:

When a farming or other self-employment business is connected to or on the same property as the client's home, a breakdown of farm/business shelter expenses (e.g., rent or mortgage) from personal shelter expenses must be made. Do not allow questionable expenses when the client cannot or will not provide proof of separate business and personal shelter expenses.

In-Home Self-Employment Business:

If a self-employed client, who operates their self-employment business from their home, wants to claim part of their shelter expense as a business deduction, the personal shelter expenses must be separated from the business expenses. Only the expenses for the portion of the home that is exclusively used for the business are allowed.

Home shelter costs may be allowed as a business deduction, if the client spends a significant amount of time conducting business activities in the home; and, if the business is NOT related to dependent care, ONE of the following may be allowed:

1. The expense for a portion of the home used exclusively for self-employment inventory storage;
or
2. The expense for the portion of the home that is used exclusively to conduct business activities (the space cannot be used for any other purpose).

Shelter expenses are not allowed when the majority of income is made outside the home and the home is used only for administrative purposes.

Determining Allowable Shelter Expense:

A breakdown is determined using one of the following:

1. The client's expense calculation;
2. Amount listed on the client's IRS form 8829 (when home used for dependent care or inventory storage) or other income tax form;
3. Expense verifications the client provides (for business connected to/on home property); or
4. The ratio of business square footage to square footage of entire home (for dependent care or other in-home business).

The expense amounts listed on income tax forms is considered valid, and is only questioned if the information appears inaccurate, such as the client's entire shelter expense is deducted. If this happens, the expense can be recalculated as listed above, or with the client's consent, can be valued using vendor/in-kind policy in Section 501-1.

Non-Allowable Expenses:

Non-allowable expenses are added back into self-employment income when listed on tax forms, or are not deducted when calculating monthly self-employment income.

Examples of non-allowable expenses include:

1. Purchase costs of capital assets or durable goods, whether or not set up on a depreciation schedule. Durable goods and capital assets are business items expected to last a long time and include farm machinery, equipment, buildings, computers, swing sets, cribs, DVD players, furniture, high chairs, vehicles, hair dryers, tricycles, etc. All items purchased prior to a business opening are capital expenses.
2. Principal portion of loan repayment – the interest payment on a business loan may be deducted;
3. Federal, state, and local income taxes,
4. Transportation to and from work – the cost of commuting to the business from home is not allowed, including the cost of commuting to the job site if the business does not have a set place of business. **EXCEPTION:** When the client is transporting tools/supplies necessary to work at the job site (i.e., a "loaded" trip), transportation costs may be claimed.

BUDGETING:

Self-employment income and expenses are always annualized; expenses are allowed when paid, not when billed. The period the income is intended to cover is not considered. **NOTE:** When the client reports their self-employment business has ended, the annualized income is end-dated.

Income tax forms are used for annualized self-employment, if available. Use the most current tax forms unless the client expects a substantial change in their business or income. **NOTE:** Substantial changes include starting or ending a business; increasing or reducing business operations, etc.

If tax forms aren't available, the income is still annualized, but other documentation must be provided to determine annualized income.

NEW BUSINESS:

Determine income for a new business by averaging the income and expenses for the months the business has been in operation.

If there is no reliable history, the eligibility staff member and the client must agree on a reasonable projection.

RENTAL INCOME:

Rental income may be earned or unearned depending on whether or not the client is materially participating in the rental business (see 'Activities that are Not Self-Employment' in this section for more information), and is determined on a case-by-case basis. The cost of business is deducted to determine net income for both earned and unearned rental income.

ROOMER INCOME:

Countable. Roomer income may be earned or unearned depending on whether or not the client is materially participating in the business. If the client is materially participating, treat roomer income as earned self-employment. When the client is not materially participating, roomer income is unearned.

Earned and unearned roomer income is offset based on prorated household expenses (i.e., the home has 5 total rooms, excluding bathrooms and attics/basements (unless converted to living spaces) and the roomer rents one room; 20% of the household shelter expenses are allowed).

BOARDER INCOME:

Countable. Commercial boarding houses are treated as regular self-employment. Boarding situations that are not in a commercial boarding house may be earned or unearned depending on whether or not the client is materially participating in the business and are treated as follows:

- Boarder income includes all payment made directly to the household, including payments for meals and shelter. Countable income is determined by subtracting the household's costs of providing room and meals from the total boarder income received.

Use one of the following methods to determine allowable expenses:

1. Actual documented expenses for room and meals, and pro rata share of food, utilities, etc.; or
2. Amount allowed for vendor/in-kind food and/or shelter (see 'Vendor Payments' in 501-1); or

3. **ABD:** One-third value reduction provision (see 'Vendor Payments' in 501-1).

SELF-EMPLOYMENT LOSSES:

ACA: Any loss reported on Schedule E, Line 32 can be used to offset any other income and decrease MAGI income.

ABD and Family Medically Needy: Subtract verified self-employment losses from other self-employment gains.

ABD: Self-employment losses can also be deducted from other earned income.

BANKRUPTCY:

Continue to use the projected monthly self-employment income until the client reports the business will have a substantial change in income and/or expenses. A statement from the bankruptcy trustee can verify the debt reorganization plan. Continue to count the self-employment income even when it's diverted to a bank or other source. Deductions for trustee or conservator's fees are not allowed. When equipment or land is repossessed or title is given to the lender, the property is no longer owned by the client; sale of this property is not considered income. A loan that is forgiven or written off is not considered income.

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