

Internal Revenue Service

New Business Workshop

Volunteer Workshop Presenter

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Before You Go

Please submit your comments about this
workshop on my website

www.LarryHesscpa.com

Topics

- « Taxpayer Identification Number
- « Recordkeeping
- « Retaining Tax Records
- « Self-employment tax
- « Estimated Taxes
- « Employee or Independent Contractor?

Record

Taxpayer Identification Number

Keeping

Taxpayer Identification Number

**Social Security Number
from Social Security
Administration**

Format *000-00-0000*

**Employer Identification
Number (*EIN*) from IRS**

Format *00-0000000*

To Obtain New EIN

§ IRS.gov

- Search for "EIN"
- Receive EIN immediately
- *Tip*: Print onscreen confirmation

§ Fax Form SS-4 1-215-516-3990

- Receive by fax within about 6 weeks

Returns Business Organizations File

1/9/2022

New Business Workshop

What Form Must Be Filed?

Taxes paid with return

- Sole Proprietorship *Schedules C & SE*
- Corporation *Form 1120*

Taxes paid by owners (aka pass-thru entities)

- Partnership *Form 1065*
- S Corporation *Form 1120S*
- Limited Liability Company *It depends*

Pub 583
Page 3

Tip: Obtain advice from a competent tax professional and attorney when considering the appropriate type of entity for your business.

Record

**Recordkeeping
&
Bookkeeping**

What's the Difference?

Recordkeeping

Documentation required to prove entries on tax return

Bookkeeping

System used to compile category totals

Why Keep Records?

Good records are required to ...

§ Prepare tax returns and support items reported on tax returns

What Must Be Proven?

P All income is taxable unless you prove otherwise

P Expenses are the opposite. You must prove you are entitled to deductions

§ You spent money

§ Payments were connected to your business

Supporting Documents

(Examples)

Income

- Deposit records
- Bank transfers
- Loan agreements
- Investments

Expenses

- Itemized receipts
- Paid bills
- Bank & credit card statements
- Cancelled checks

Information Needed for Every Payment

- ü Date
- ü Check # or other reference
- ü Who you paid
- ü What for
- ü Category of the expense
- ü Amount

Why Bookkeeping?

A good bookkeeping system can help you ...

- § Prepare financial statements
- § Monitor progress toward business goals
- § Identify productive & unproductive income sources & expenditures

You May Use Any Bookkeeping System

- Ø *Pile of Receipts* (ok, but ...)
- Ø *Handwritten Ledgers* (good)
- Ø *Software* (best)
 - ü Spreadsheet
 - ü Checkbook app
 - ü Business app



Pile System



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IBR-3721459 - aqefotostock

Handwritten Ledger

DATE	PAID TO	CK # DE / CC CASH	PAID FOR	TOTAL PAID	MOVE- THING	AUTO- MOBILE	FURNIT- TURE & EQUIPMENT	OFFICE SUPPLIES	SOFTWARE	TELE- PHONE & INTERNET	OTHER CATEGORIES	AMOUNT
2020												
9/1	WELLS FARGO	101	CHECKS	2500								
9/1	STATE FARM	CC	BUSINESS INSURANCE	3000							MOVES	3000
9/2	COSTCO	AD	COMPUTER PAPER, PENS, ENVELOPES MEMBERSHIP GAS FOR HOME	1465			10500	7500			TOYS PERSONAL	9000 15000
9/3	MTRIT	CC	QUICKBOOKS	2000						2000		
9/3	CENTURYLINK	DE	INTERNET MIDEM	1500				10000				
9/4	T-MOBILE	CC	CELLPHONE SERVICE SAMSONITE MACHINE	3500				30000				
9/5	GOOGLE	DE	GOOGLE AD -	2500	2500							
9/5	US POSTAL SERVICE	CC	STAMPS	1100							POSTAGE	1100
9/8	GOODWILL	DD	DESK + CHAIR	3000								
9/9	FLEA MARKET	CASH	DESK LAMP	2500				2500				
9/8	STAPLES	CC	SURETYER	9000				9000				
9/8	SPEEDWAY	DL	GAS FOR HOME	3500		3500						
9/10	AMAZON	CC	BOOKS & OFFICE	1500								
	TOTALS			34000	2500	3500	10500	10000	2500	10000		

Some Best Practices

- Don't mix personal and business income and expenses
- Open separate bank and credit card accounts for your business
- Always deposit cash received
- Never take cash back from deposits
- ATM withdrawals and checks payable to "cash" are not deductible until the cash is spent

Record

Saving Your Tax Records

Keeping

How Long To Save Tax Records

Save documentation supporting entries on tax returns for *as long as the returns can be audited*.

IRS: 3 years after filing deadline or actual filing date, whichever is later.

- N.M.: Dec. 31 of third year after return is *due*

Exceptions

- ü 6-years under certain circumstances
- ü Tax returns - forever
- ü Capital assets - almost forever

Capital Assets

- ü Asset expected to have a useful life longer than a year and is not intended for sale in the regular course of the business's operation.
- ü Amount of deduction and timing is determined by rules for depreciation.
- ü Documentation of purchase must be retained until 3 (or 6) years *after last year subject to depreciation rules.*

Taxes Affecting Businesses

Record

Income Tax

(Everyone knows about this one)

Receipt



Taxes Affecting Businesses

Record

Payroll Tax

(IRS New Employer Workshop)

Receipt



Taxes Affecting Businesses

Self-Employment Tax

(Social Security and Medicare)



Important For Self-Employed People

Be prepared to pay tax owed

- Self-employment tax can be considerably more than income tax
- Direct payments to the IRS include income tax
- No withholdings to help pay

Calculating Self-Employment Taxes

Paid on net earnings from self-employment

- Sole proprietors
 - Net profit shown on Schedule C
- Partnerships & multi-member LLCs
 - Income on Schedule K-1 given to owners
- Use Schedule SE to calculate

Self-Employment Tax vs. Income Tax

(Example using 2020 rules)

Business net profit		\$44,200
Standard deduction (2 x \$12,400)		-24,800
Exemptions (4 x \$0)		0
Total deductions		-24,800
Taxable income		19,400
Income tax	10.0% x 19,400	1,940
<i>Self-employment tax</i>	15.3% x 44,200	6,586
Combined tax		8,526



Pay on Time

Pay by April 15

- Not affected by extension

If you pay late

- Penalty 1/2% per month on any amount paid after April 15 (*maximum of 25%*)

Consequence

- You may need payment plan
 - Challenging to pay current year taxes & back taxes at same time

Taxes Affecting Businesses

Estimated Tax

(Quarterly Payments)

Estimated Tax Is Not A Tax

- ü Prepayments of current year tax
- ü Paid with direct payments to IRS
- ü Each payment is combination of income and self-employment taxes
 - Amount of each tax is not specified

Prepayment Requirement

General rule

- ü Prepay 90% of current year tax in 4 equal payments due

April 15 - June 15 - September 15 - January 15

- ü Federal tax withheld from paychecks treated as if paid equally throughout the year

Minimizing Penalty for Underpayment Estimated Tax

- No penalty if 100% of prior year total tax is paid in current year *(with limitations)*
- Payments can be matched to fluctuations in sales during the year

When Estimated Tax Payments Are Not Required

Individuals

- Expect to owe less than \$1,000 when you file your return.

Corporations

- Expect to owe less than \$500 when corporate return filed.

One Way to Determine Approximate Tax If Income Is Variable or Unpredictable

Based on Business Gross Receipts

Total tax	\$8,526
<i>(From self-employment tax example)</i>	

Divided by	÷
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Business gross receipts	100,000
<i>(From Schedule C, line 1 or CRS-1s)</i>	

Federal tax cost related to sales	8.5%
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Tip: Using gross receipts reported monthly to N.M. Taxation & Revenue Dept. is a good reminder of when to calculate federal estimated tax payments.



Consequence of Not Prepaying Required Amount on Time

Penalty for underpayment of estimated tax

- § Currently 3% of required
payment amount for number
of days not paid**
 - 1.7% effective maximum if no ES
payments are made**

3 Ways To Pay

Online (best)

- ü Go to www.irs.gov
- ü Click "Make A Payment"

Check

- ü Mail with Form 1040-ES
(1040-V after April 15)

Electronic Federal Tax Payment System

- ü EFTPS.gov

Estimated Tax – New Mexico

New Mexico also has estimated tax payment requirements similar to the federal rules

Employee
- *or* -
Independent Contractor?

Making The Decision

- § Not a voluntary choice
- § Must be made using facts and circumstances surrounding the work relationship of each worker
- § Sometimes misunderstood
 - “I’m the only person in my business”
- § There can be temptations to ...
 - ü "1099" workers to save costs and simplify administration
 - ü Go along with a worker's request to avoid withholdings

Worker Status Types

Employees

- Under your direct control

Independent Contractors

- Not under your direct control
- People who are *in business* for themselves are not considered employees
- Perform services for your business

Cost of Having Employees

Cost of employer taxes

- ü As much as about 14% of wages

Payroll taxes

- ü Employer must match withheld Social Security and Medicare taxes (7.65%)
- ü Unemployment tax (up to 5.4% in N.M.)

Workers' compensation insurance (may be required)

Discretionary costs

- ü Employee benefits (examples)
 - Health insurance
 - Retirement
 - Paid vacation

Cost of Misclassifying Workers

§ Employee withholding taxes	7.65%
§ Employer payroll taxes	7.65%
§ Late filing penalty (per month)	5%
§ Late payment penalty (per month)	½%
§ Failure to deposit penalty	10%
§ Interest (per annum)	3%
§ <i>Total approximately</i>	<i>34%</i>

Worker Recourse

Workers who believe they have been misclassified as independent contractors have recourse

- § Report to IRS using Form SS-8, *Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding*
- § File unemployment or workers compensation claim

Making the Decision

Three general categories of factors to consider:

- ∅ Behavioral *control*
- ∅ Financial *control*
- ∅ Type of relationship

20 Factors IRS Considers When Evaluating Worker Status

	EE	IC
Type of instruction		
Amount of training		
Degree of business integration		
Extent of personal services		
Control of assistants		
Continuity of relationship		
Flexibility of schedule		
Demands for full-time work		
Need for onsite services		
Sequence of work		
Requirements for reports		
Method of payment		
Payment of business or travel expenses		
Provision of tools and materials		
Investment in facilities		
Realization of profit or loss		
Work for multiple companies		
Availability of public		
Control over discharge		
Right of termination		

Behavioral Control Factors

Facts that illustrate whether there is a right to direct or control how the worker performs the specific task for which he or she is hired:

- P** Degree of instruction
- P** Training

Behavioral Control Factors

Types of instructions given

- P** When and where to do the work.
- P** What tools or equipment to use.
- P** What workers to hire or to assist with the work.
- P** Where to purchase supplies and services.
- P** What work must be performed by a specified individual.
- P** What order or sequence to follow when performing the work.

Financial Control Factors

- P** Unreimbursed expenses
- P** Opportunity for profit or loss
- P** Significant investment by worker
- P** Services available to the market
- P** Method of payment

Relationship of the Parties

- ü Employee benefits
- ü Intent of the parties/Written contracts
- ü Permanency of the relationship
- ü Discharge/Termination
- ü Regular business activity

IRS Resources

- Search IRS.gov for “small business”
 - Select link for Small Business and Self-Employed Tax Center
- Publication 334, *Tax Guide for Small Business (For Individuals Who Use Schedule C)*
- Publication 535, *Business Expenses*
- Publication 583, *Starting a Business and Keeping Records*

Where to Find Us

Online

www.irs.gov

Business and Specialty Tax Line

1-800-829-4933

TELE-TAX

1-800-829-4477

TTY/TDD

1-800-829-4059

Albuquerque Office

7200 Jefferson St. NE

Note: Appointments are required for individuals needing face-to-face service at the Taxpayer Assistance Center for all matters except for making payments. Make appointments by calling 844-545-5640.

There's more on my website

www.LarryHesscpa.com

- ü Share your feedback about this workshop
- ü Register for my other workshops
 - *Essential N.M. Gross Receipts Tax*
 - *Basic (very basic) Bookkeeping*

Your Questions?



**What more
would
you like
to know?**