

TaxTips

For Small Business

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JAMES E. GEORGE, CPA PA
4014-B MOUNTVILLE ROAD
JEFFERSON, MD 21755
301-473-4445 FAX 301-473-4449

Audits are on the increase. Could you be at risk?

IRS and State of Maryland both targeting non-compliance!

Accountants are starting to see a significant increase in the number of audits of their clients. The IRS is targeting issues of non-compliance. The State of Maryland is looking for money to solve their budget crises.

The IRS is auditing income tax returns that involve issues they have found to be out of compliance on many returns in prior years. Issues such as business use of a personal automobile, home offices and treating employees as subcontractors are receiving special attention. The audits usually result in the business owner being assessed additional tax and a hefty amount of penalties and interest. What can you do to minimize your audit risk?

Documentation of auto related expenses is a must. Maintaining an accurate log of business mileage that can be verified by other receipts and records will help safeguard your auto deductions. Receipts for all business expenses should be kept in an organized system of files whenever possible. A home office should not be claimed unless it meets the specific criteria for deduction. Anyone who provides services to your company on a regular basis may be deemed an employee. Though it is simpler to treat them as a subcontractor and not withhold taxes, the IRS and the state have regularly reclassified these people as employees. The result is a sizeable payroll tax assessment. The criteria for determining a workers status can be found in the IRS publications, or you may contact our office.

The State of Maryland has increased their sales and use tax audits. They are looking for items used by businesses that were purchased out of state and brought into Maryland without any sales tax being paid. They also are looking for items purchased with a resale certificate that are being consumed by the purchaser. These types of liabilities are referred to as "Use tax." It is important for a business owner to track their Maryland sales tax liabilities for untaxed purchases of items used by the business. Items for resale to customers are not subject to the tax.

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Our office has handled a significantly higher number of state unemployment audits over the past six months. The State of Maryland has found a source of revenue and they are starting to generate significant assessments by auditing small businesses that use subcontractors and casual labor. The states' definition of an employee is much broader than the IRS definition. Thus, a person may qualify as an independent contractor for federal purposes but will be considered an employee for the assessment of state unemployment tax liabilities. This could create problems at the end of the year when the federal and state governments compare gross wage figures reported on W2's versus quarterly returns!

To protect yourself and your business from unexpected assessments we recommend you obtain the workers name, address and social security number before you allow them to start working. This is the law. We also recommend you consult the IRS publications for guidance or you may call our office and schedule a consultation. We can inform you of the rules and requirements and explain what documentation you need to have in your files to protect yourself in case the auditor comes calling!



Hire Your Children for the Summer

Save your business some payroll taxes

There are benefits to hiring your children to work for you. If your children are under the age of 18, you are not required to withhold social security and Medicare taxes from their wages. You are also not required to pay federal unemployment taxes on their wages until they reach the age of 21.

Only self-employed business owners can take advantage of this benefit. Partnerships are included in this category as long as the parents are the only partners. If your business is incorporated, the children are considered employees of the corporation, and are subject to the normal payroll taxes regardless of their age.

Many of our clients will be faced with paying thousands of dollars for their children's college education expenses. If a business owner were to employ their child from the ninth thru twelfth grades, pay them \$8.00 per hour for working sixteen hours per week, they could accumulate over \$20,000.00 toward college before they graduate from high school! Writing this amount off as a business expense would save the parents around \$9,000.00 in income taxes during the child's high school years.

Your child's employment should be documented as if they were an unrelated party. Time records must be maintained documenting the hours worked and duties performed. Employment forms should be completed and maintained in their employee file. You cannot simply give your child money and deduct it through your business.

The additional benefits of teaching your children business fundamentals and helping them to see firsthand the importance of good customer service will benefit them throughout their working careers.

Changes in Estimated Taxes for Small Businesses

Reduced required estimated tax payments

If your income is primarily generated from operating a small business in 2009, you may be eligible for reduced required estimated tax payments. A new law allows you to base the computation of the 2009 estimated payments on 90 percent of your 2008 income tax liability instead of 100 percent. In order to qualify for this reduced amount, your adjusted gross income must be less than \$500,000; in addition, more than 50 percent of the gross income shown on your return for the prior year has to be income generated from operating a small business. A small business is defined as a trade or business with an average of 500 or fewer employees.

Meal Rates for Day Care Providers

Keeping track of meal expenses is easier than ever

If you provide day care services in your home, some of the most difficult expenses to track are meals. The IRS has made it easier for you by allowing a standard meal allowance that can be used in lieu of actual expenses. The chart outlines the meal rates allowed for 2009.

Meal	Alaska	Hawaii	All Other States
Breakfast	\$1.86	\$1.36	\$1.17
Lunch/Dinner	\$3.53	\$2.55	\$2.19
Snack	\$1.05	\$0.76	\$0.65



Starting Your Own Business

Tips for turning a hobby into a profitable business

With the economy the way it is today, jobs are hard to find. Starting your own business might be the only way to earn a living. You have to have a good idea, map out all the details needed to put it into operation, and be firmly convinced of your ability to make it work. Having it all worked out in your head is one thing, but it's only when you take the time to create a written document that embodies your thoughts that you realize the scope and magnitude of what's involved in running a business. In your head, you've concentrated on the idea. In your business plan, you can examine the nuts and bolts of running a business to make the most of your idea.

A well developed plan can serve as one of your most important management tools. A good plan will provide a blueprint and step-by-step instructions on how to translate your idea into a marketable service or product. Once the business plan is in writing, you need to follow it so you can stay on track and avoid costly mistakes. It might also help when it comes time to find investors.

You'll also need to develop a marketing plan. You won't sell your product or service unless the public knows you exist. The Internet has become a great place to advertise your business, and the costs you incur are deductible as advertising expenses once the business is open.

There are several different forms of business entities: corporations, partnerships, sole proprietorships, and limited liability companies (LLCs). What type of entity should you choose? Getting good advice from your tax professional prior to starting any business activity will save you time and money later.

COBRA Premium Subsidy

Involuntarily separated employees can elect to pay only 35 percent of COBRA coverage

A new law allows individuals who are involuntarily separated from employment between September 1, 2008, and January 1, 2010, to elect to pay 35 percent of their premium for COBRA coverage and have it treated as being paid in full.

The former employer will be required to pay the other 65 percent and will be reimbursed through the filing of Form 941. The amount will be credited against income tax withholding and payroll taxes the employer is otherwise required to remit to the federal government. The maximum period for which the subsidy can be provided is nine months.

QUICK TIPS

1 The expense deduction for business equipment purchased in 2009 remains at \$250,000.

2 Instead of deducting the actual expenses for the business use of your vehicle, opt for the standard mileage rate. In 2009, you can deduct 55 cents for each business mile you drive.

3 A deduction is allowed for the cost of an energy efficient building placed in service during the tax year of up to \$1.80 multiplied by the square footage of the building.

4 The Social Security wage base increases to \$106,800 in 2009, up from \$102,000 for 2008. This means that you are no longer required to withhold social security tax for employees after meeting this threshold. You are, however, required to withhold Medicare taxes regardless of the amount of wages paid.

5 If you are disposing of property used in your business, you may want to consider a like-kind exchange to defer the taxable gain on the sale.

6 If your business owns a vehicle that is available for an employee's personal and business use, the vehicle is nevertheless considered used 100 percent for business on the business tax return. The personal-use percentage is included on the employee's W-2 as additional compensation.

7 Employer-provided education assistance benefits of \$5,250 provided under a written plan are excludable from wages. The education need not be job-related to qualify.

8 If you are planning on starting a SIMPLE retirement plan for yourself or your employees, do it now. The deadline for setting up a SIMPLE plan is October 1, except if you are a new employer coming into existence after October.

Choosing an S Corp or an LLC as a Form of Doing Business

Many business advantages and disadvantages make these options a tough choice

A subchapter S corporation is a business entity separate from its owners. It provides a level of liability protection similar to a regular corporation without the double taxation of its income. An S corporation can insulate its' owners from lawsuits and creditors in most cases. One advantage of an S corp. over an LLC is it has a perpetual existence and does not have to fold when the company is sold. Another advantage is the earnings of a subchapter S corporation are not subject to the 15.3% self employment tax that most LLC members have to pay. On \$30,000 of profit this will result in a tax savings of \$4239!

S corporations aren't necessarily the entity of choice in all scenarios. If real estate is involved an LLC may be a better choice. This is because LLC sales of real estate are taxed as capital gains on the members' personal income tax returns whereas a corporation treats the gains on the sale of real estate as ordinary income.

A limited liability company (LLC) is a business entity separate from its owners. The major advantage is that it allows owners to participate in the management and to take advantage of the pass-through taxation while limiting their liability for debts or the business. LLC members have limited liability that is usually only common in corporations.

A single member LLC is taxed as a sole proprietorship by default; an LLC with two or more members is taxed as a partnership by default. Either LLC can elect to be taxed as a corporation.

The other attributes of the LLC usually will be determined by how the LLC is taxed. An LLC taxed as a corporation follows the corporation rules; an LLC taxed as a sole proprietorship follows the sole proprietor provisions; and an LLC taxed as a partnership follows the partnership rules. For example, an LLC taxed as a sole proprietor will not issue a Form W-2 to the single member for services provided, because a sole proprietor cannot issue a Form W-2 to himself or herself. The same is true for an LLC taxed as a partnership; members will not receive a Form W-2 from the partnership. However, an LLC taxed as a corporation will issue a Form W-2 to a member who provides services.

Both S corps and LLC's are formed under the laws of the state where the business is conducted. An LLC's Articles of Organization usually define who will be responsible for managing the company. The S corps Articles of Incorporation are usually silent as to management thus providing a level of privacy.

Our office offers both counseling as to choice of entity and assistance with forming your company.

Solo 401(k)

Option increases retirement savings

If you're the sole owner of a business, you may wish to consider the implementation of a solo 401(k) retirement plan to accumulate retirement savings on a tax-deferred basis.

Self-employed taxpayers can contribute to a solely owned 401(k) retirement plan as both employer and employee. As an employer, you can contribute up to 25 percent of your total net earnings to your retirement plan; as an employee, you may also contribute an additional \$16,500 in 2009. If you are age 50 or older, you can contribute an additional \$5,500 for a total of \$22,000.

Your maximum contribution to a solo 401(k) plan is the lesser of \$49,000 or the sum of your employer and employee maximum contributions. The solo 401(k) plan provides you with an additional opportunity to maximize your yearly retirement contribution. As an added bonus, this type of plan, unlike other retirement plan options, allows participants to take out loans from the plan.

The information contained in this newsletter is not intended to provide specific tax advice or to take the place of either the written law or regulations.

