

# YEAR-END COMPILER



**An organizer with year-end tips for the sole proprietor**

## Time to get organized

It's time to pay Uncle Sam for what you have made. This organizer is designed to help you compile the information for Schedule C.

As a small business owner, you are the cornerstone of America, one of 15 to 20 million of them, that is.

You will pay income tax **and** self employment tax on gross income minus allowable expenses.

By following the three steps below and using the tips along the way, you should be able to save tax dollars.

You may be the cornerstone of America, but you do not want to be the whole foundation when it comes to paying tax.

**If you look at Schedule C, you will notice three sections, which we will cover in 3 easy steps:**

**Step 1: Who are you?**

**Step 2: How much did you make?**

**Step 3: How much did it cost you to make the money?**

## Who are you?

Uncle Sam wants to know who you are, where you operate, and what you did to make money. If you have more than one business, you need to do a separate Schedule C for each of them..



**Use this organizer for only one business.**

Business name \_\_\_\_\_

What do you do? \_\_\_\_\_

Business address \_\_\_\_\_

How many months was your business in operation during the year?

12 months

from \_\_\_\_\_ to \_\_\_\_\_

How many hours did you devote to the business during the year?

Full time or \_\_\_\_\_

**Now that you have recorded who you are, you are ready for Step 2.**

## How much did you make?



Part 1 of Schedule C records your *Gross Income* (before deductions).

**Gross Receipts** are the income you receive from your business. You should have evidence to support these receipts. The law does not require you to keep any certain kind of record as long as the method you choose clearly shows your income and is consistent.

Some examples of methods are printed below. Enter your **gross receipts** next to the method you used.

_____ Cash Register Tapes	_____ Invoices
_____ Bank Deposits	_____ 1099 Forms
_____ Record Books	_____ Other (explain)
_____	

## Cash or accrual?



There are two basic methods of accounting. Most small businesses use the cash method.

**Cash method:** With the cash method, income is recorded as you receive it. Expenses are recorded as you pay them.

**Accrual method:** With the accrual method, income is reported when you earn it even if you haven't received it yet. Expenses are recorded when you owe them even if you haven't paid them yet.

Which method did you use to record your gross receipts?

- Cash                       Accrual

**TIP:** To reduce your **Gross Income**, delay your December billing to customers to defer it to January. Be aware of the term **constructive receipt** which means money is yours when you have a right to receive it. That is, if you have money, but have not yet deposited it in the bank, you have income.

## Did you sell a product?

If you sold or manufactured a product you need to figure the cost of the goods you sold. Basically, you can only deduct the items you purchased or made **and** actually sold.

Separate into the following categories the costs associated with the items sold to customers from the rest of your expenses:

- \_\_\_\_\_ Purchases of items for sale
- \_\_\_\_\_ Items withdrawn for personal use
- \_\_\_\_\_ Purchase of manufacturing material
- \_\_\_\_\_ Labor paid for manufacturing
- \_\_\_\_\_ Other production costs
- \_\_\_\_\_ Packaging

Now that you have separated the costs of the items you held for sale to customers, you need to determine year-end inventory. There are many methods for doing this. A physical count is common.

- \_\_\_\_\_ Year-end inventory ( How much is left at the end of the year - at your cost) *or*, if it's too late to spend New Year's Eve counting
- \_\_\_\_\_ What was the cost to you of each item you sold?
- \_\_\_\_\_ If you use this method, also calculate the cost of lost, stolen, or broken items.

**TIP:** Since you can't deduct it until it's sold, reduce your year-end inventory by destroying dead stock (keep evidence), or giving it to charity.

**Now that you have recorded your gross income, you are ready for step 3.**

## What did it cost you to make the money?

What expenses are deductible? The two key words to remember are **ordinary and necessary**. Internal Revenue Code Section 162 states:

*There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business. ...*

## Where to begin?

Begin by collecting whatever evidence you have of **ordinary and necessary** expenses. You may have any one of the following:

- Bag or box of receipts
- Canceled checks
- Check carbons
- Itemized computer printout

If you have the printout, the task ahead will be simple. Just read through the following lists to make sure you haven't missed anything.



If you have receipts and checks, you will need to create a computerized printout or sort the evidence into piles according to category and add them up. Then check the list for more.

If you started your business this year, separate the expenses paid for before business began and enter here: \_\_\_\_\_ Equipment  
\_\_\_\_\_ Inventory \_\_\_\_\_ Other expenses

## Ordinary and necessary expenses

The following list is not all-inclusive for every taxpayer. An ordinary expense for one business may not be ordinary for another.

**Advertising/Promotion:** Ads, bus. cards, holiday cards. (Uncle Sam doesn't mind seeing a large number here).

**Car and truck expenses:** see separate section

**Commissions and fees:** include contract labor here. If you paid over \$600 to one individual for services rendered, you must prepare a 1099.

**Equipment purchased:** see equipment section

**Employee benefits:** Health ins., holiday or employee party, mileage reimbursements, parking and mass transit benefits...

**Insurance:** Workers Comp., business liability, malpractice, ... (not auto, health, home)

**Interest:** Mortgage on business building, equipment loans, business loans, business-only credit card.

**Legal and Professional:** Attorney and accounting fees, bonds, consulting, secretarial... If you paid over \$600 to an individual, you must make a 1099.

**Office expense:** postage, stationery, office supplies, bank charges, printing and copying, pens, ....Do not include equipment here. If this category gets large, break it down into sub-categories.

\_\_\_\_\_ **Pension and profit sharing plans** for employees.

\_\_\_\_\_ **Rental/ lease of equipment**

\_\_\_\_\_ **Rental of other business property:** office space, storage, land....

\_\_\_\_\_ **Repairs and maintenance:** to building and equipment (do not include auto, home)

\_\_\_\_\_ **Supplies:** trade supplies, small tools, expendable non-office items.

\_\_\_\_\_ **Taxes and licenses:** personal property taxes, business licenses, real estate taxes (not your home)

\_\_\_\_\_ **Taxes/ Sales Tax:** include if Sales Tax is included in gross receipts.

\_\_\_\_\_ **Taxes/ Payroll**

\_\_\_\_\_ **Travel:** see travel section

\_\_\_\_\_ **Meals and entertainment:** Business meals and tickets to events are 50% deductible. You must have a record of who, where, when, and why.

\_\_\_\_\_ **Telephone:** business line, second line (the first line coming into your home is not deductible), phone enhancements, fax transmissions, pager, cell phone (business %)

\_\_\_\_\_ **Utilities:** electricity, heat, garbage, water (do not include home office expenses here).

\_\_\_\_\_ **Wages:** Include gross wages from W-2's.

\_\_\_\_\_ **Alarm service**

\_\_\_\_\_ **Answering service**

\_\_\_\_\_ **Bank charges** if not already listed elsewhere.

\_\_\_\_\_ **Books**

\_\_\_\_\_ **Credit card charges**

\_\_\_\_\_ **Courier/ delivery services**

\_\_\_\_\_ **Conventions/ meetings**

\_\_\_\_\_ **Dues and publications**

\_\_\_\_\_ **Education/ seminars**

\_\_\_\_\_ **Fuel for equipment** (not auto)

\_\_\_\_\_ **Gifts** (limit of \$25 per person)

\_\_\_\_\_ **Laundry and Uniforms**

\_\_\_\_\_ **Postage**

\_\_\_\_\_ **Show fees**

\_\_\_\_\_ **Other** \_\_\_\_\_

**TIP:** The best defense in case of an audit is a business checking account with all income consistently tracked. If you do not have one, make sure the method you use is substantiated beyond doubt. Using a bank account to track income is cheap, efficient, and essential if you want your business to grow.



## Do you work in your home?

If you have an area in your home that is regularly and exclusively used for business, you may benefit from the home office deduction. Your office must be one of the following: Your principal place of business, a place you meet customers, a place where you store inventory for resale, or a place where you conduct administrative activities.

To take the home office deduction you will need the following:

\_\_\_\_\_ Date you acquired the home

\_\_\_\_\_ Total cost of the home

\_\_\_\_\_ Cost of the land

\_\_\_\_\_ Cost of improvements

\_\_\_\_\_ Square footage of the home

\_\_\_\_\_ Square footage of the office area

\_\_\_\_\_ Mortgage interest

\_\_\_\_\_ Property taxes

\_\_\_\_\_ Insurance

\_\_\_\_\_ Repairs and maintenance

\_\_\_\_\_ Utilities

\_\_\_\_\_ Rent paid (if you rent)



Using the above information, a business percentage is obtained. All expenses are multiplied by that percentage and depreciation is calculated. When the home is sold, all depreciation taken since 5/7/97 must be taxed. Also, on the down side, when the home is sold, if you do not have 2 of the last 5 years without home office, the business percentage of the gain will be taxed.

**TIP:** If you are considering selling your home in the near future, avoid the home office so you can meet the 2-year test.

**TIP:** If a home sale is not in your future or you are a renter, the home office is a good idea. It will enable you to deduct more business miles. (see below)

## Do you use your vehicle?

Business mileage requires special recordkeeping. A daily log or record is essential.

### What mileage qualifies for a deduction?

You can use one of the following three scenarios to determine how many miles you can deduct. Keep in mind that **commuting is not deductible**.

**If you have an office or regular place of business outside your home,** you may not deduct commuting miles to and from work or to your first and from your last stop home, but you may deduct mileage to a temporary work place and mileage to drive to and from different locations during the day.

**If you have an office in your home that qualifies for a home office deduction,** all of your business-related mileage is deductible.

**If you work at your home, but do not qualify for the home office deduction,** the distance between home and your first stop and between your last stop and home are nondeductible commuting miles. You should plan to have your first and last stops close to home to maximize the mileage deduction. A trip to the bank, gas station, post office, or a nearby supplier can help increase deductible business miles. **The proof is in documentation.**

## Deducting mileage

Now that you know what miles to count, you need to choose one of the two methods of deduction. Whichever method you use, you will have to know the following:

_____	Year and make of the vehicle
_____	Date purchased
_____	Business miles driven
_____	Total miles driven
Beginning odometer _____	(January 1)
Ending odometer _____	(December 31)
_____	Total miles commuting to work
_____	Parking and tolls
_____	License plate fees
_____	Loan interest

**Standard mileage rate:** The IRS has a standard mileage rate you can apply to your business miles driven. It is subject to change yearly. Also, you may deduct the business percentage of license plates and loan interest, plus all of your business parking.

**TIP:** In general, the standard mileage rate works best if your business mileage is high or your car is economical to operate.

**Actual expense method:** You may deduct the business percentage of all expenses plus parking and depreciation. The following additional information is needed:

_____	Cost of the vehicle	_____	Insurance
_____	Gas	_____	Supplies, washes, waxes...
_____	Oil, lube	_____	Lease payments
_____	Repairs, tires, batteries		

**TIP:** The actual expense method works best if your vehicle weighs over 6000 pounds, is costly to run, or you do not drive many miles in total.

**TIP:** If you keep an appointment book, it already shows where you went, so you can write a mileage total on each day without keeping a separate book.

## Did you buy equipment?

**The bad news:** If you bought property that you expect to last longer than a year, you must depreciate it.



**The good news:** You can elect to expense some or all of these purchases each year.

List your purchases of equipment for the year below. Check through your lists of office expenses and supplies for items that might fall into this category.

Item purchased	Date purchased	Cost
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____

## Did you travel for business?

You may deduct ordinary and necessary living expenses incurred when you are away from your tax home overnight for business. Your travel records must show the following information: Dates and times of arrival and departure, number of days actually spent on business, business places visited, and business reason for travel.

The following items can be deducted:

_____	Transportation
_____	Meals
_____	Business phone calls
_____	Laundry and cleaning
_____	Cab/ local transportation fare
_____	Lodging
_____	Tips and baggage
_____	Other ordinary & necessary expenses



Instead of deducting the actual cost of meals, you may use the standard meal rate which varies from city to city. Indicate the cities to which you traveled and the nights you spent in each city.

city _____	nights out _____
city _____	nights out _____
city _____	nights out _____
city _____	nights out _____
city _____	nights out _____

## It's complete!

Your business information is now ready for your tax appointment. This compiler only touches on the many ways you can make the tax law work for you. Your tax preparer will help you customize the information to your situation.