

13.0 Taxation Issues

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13.1 Introduction and Summary

With serious cost implications, the importance of tax strategies for a small business cannot be overstated; tax avoidance will often be a prime consideration in developing an organizational structure.

13.2 Taxation Issues

It is prudent as part of setting up a new business to engage a tax professional.

The courts have held that there is nothing sinister in arranging one's affairs to keep taxes at a minimum.

A Federal Tax ID number (EIN) is required for every business. For a Sole Proprietorship, the Social Security Number serves as the EIN. An EIN can be obtained from the IRS over the telephone, but a form SS4 should be completed first.

A Business Tax Kit is available from the IRS.

What is **taxed**:

- Net profit from a Partnership, Subchapter "S" Corp. or Limited Liability Company is included with other income on Form 1040.
- Profit from a Corporation is **taxed to the Corporation**, then is retained within the company or paid out to the stockholder as dividends, which is taxable to the shareholder. Profits from a "C" Corporation are taxed twice, once at the Corporation level and again at the individual level on the dividends paid. Net losses can be carried forward or backward.

Quarterly tax returns may be required by both the Federal Government and the State of California. See Form 941 and CA Form DE6.

If company pays an **independent contractor** more than \$600/year, a form 1099 is required. Independent contractors are responsible for filing their own tax return.

When hiring employees, the business is responsible for deducting these taxes from wages and submitting these amounts to the Federal Government:

- FICA
- Self Employment Tax
- Federal Unemployment Tax
- State Unemployment Insurance
- State Disability Insurance
- State Unemployment Training Tax

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13.3 Requirements for Filing a Federal Tax Return

If you are a U.S. citizen or resident, whether you must file a federal income tax return depends upon your gross income, your filing status, your age, and whether you are a dependent. For details, see IRS Publication 501, *Table 1* (see below) and *Table 2*. The filing requirements apply even if you owe no tax.

You may have to pay a penalty if you are required to file a return but fail to. If you willfully fail to file a return, you may be subject to criminal prosecution.

To obtain Publication 501, go to the IRS web site: <http://www.irs.gov/pub/irs-pdf/p501.pdf>

Table 1. 2003 Filing Requirements Chart for Most Taxpayers

IF your filing status is...	AND at the end of 2003 you were... [*]	THEN file a return if your gross income was at least... ^{**}
single	under 65	\$ 7,800
	65 or older	\$ 8,950
head of household	under 65	\$10,050
	65 or older	\$11,200
married, filing jointly ^{***}	under 65 (both spouses)	\$15,600
	65 or older (one spouse)	\$16,550
	65 or older (both spouses)	\$17,500
married, filing separately	any age	\$ 3,050
qualifying widow(er) with dependent child	under 65	\$12,550
	65 or older	\$13,500

* If you were born before January 2, 1939, you are considered to be 65 or older at the end of 2003.

** Gross income means all income you received in the form of money, goods, property, and services that is not exempt from tax, including any income from sources outside the United States (even if you may exclude part or all of it). Do not include social security benefits unless you are married filing a separate return and you lived with your spouse at any time during 2003.

*** If you didn't live with your spouse at the end of 2003 (or on the date your spouse died) and your gross income was at least \$3,050, you must file a return regardless of your age.