Tax Tips

Here are some tips to keep in mind…

Self-employed

Self-employed professionals, contractors, and consultants are responsible for taxes and employer contributions for Social Security and Medicare. You have to consider earning extra revenue to pay the self-employment (Social Security and Medicare) tax. The self-employment tax rate is 15.3% of net profit. The rate consists of two parts: 12.4% for Social Security and 2.9% for Medicare. For 2020, the first $137,700 of your combined wages, tips, and net earnings is subject to any combinations of the Social Security part of self-employment tax. The amount has increased to $142,800 for 2021. For instance, $10,000 in profit costs $1,530.00 in self-employment tax. This is important to remember when pricing out consulting engagements, or contractor's jobs.

Accounting we will go

Thinking about starting your business on a shoestring? Great! However, think again about keeping your receipts in a shoebox. It is more effective and better business to keep a detailed report of your financial activities. Not only will this save you headaches in the long run but it can help you manage your business for the future. For instance, you can generally determine how much you spent on business expenses, generate a list of non-paying clients, or estimate your tax obligations for next quarter.

Accumulate expense receipts

Getting receipts together is a nuisance. They usually end up in car visors, or laundered once they've been left in pants pockets. All those $10 receipts for coffee and muffins you shared with clients can add up to a nice tax deduction at year-end. Same for lunches, gasoline for business travel, and items you buy at the office supply store. Remember that under current tax law, these deductions apply to businesses and self-employed individuals, not employees.

Getting mileage out of it

The Internal Revenue Service allows you to deduct 56 cents per mile traveled for business in 2021. This often adds up to a hefty deduction, especially for salespeople and contractors traveling between work sites. Keep a calendar or notebook in your car, and tally the daily miles, identifying the clients or work sites visited. Your mileage log is the best evidence if you find yourself in the middle of a tax audit. Remember that under current tax law, mileage deductions apply to businesses and self-employed individuals, not employees.

Consider a payroll service

For a reasonable fee, a payroll service will create your paychecks, deposit tax money with the federal and state governments, and file all the necessary quarterly paperwork. All you have to do is track your employees' hours and call them in. Left to your own devices, a missed payroll tax payment can become your biggest IRS nightmare.

Don't base decisions solely on write-offs

Just because the IRS allows a generous depreciation deduction for a new truck doesn't mean you should buy it. Does your business need a new truck, or other piece of equipment? The word write-off doesn't mean the government is paying for the item. If you spend $30,000 on new equipment, the tax savings could be as much as $10,000. However, you've still had a $20,000 impact to your cash flow.

Don't co-mingle funds

Your personal expenses should be paid from a personal bank account, and your business bank accounts and business credit cards should be used for business purposes only. Of course, if there is money in the business account, and the mortgage is due, it's tempting to write that check. However, to stay under the IRS radar, it's important to transfer money to your personal bank account to pay personal bills.

Save for retirement

You can borrow money to buy a home, finance a car, higher education, new appliances, just about anything. But you can't borrow money for retirement. And even though it may be 10, 20, or 30 years away, the time to act is now. There are tax advantages for contributions to your 401(k) or an Individual Retirement Account (IRA). And it doesn't have to be a big amount. You can set up monthly deductions from a bank account, or even weekly payroll deductions, which you won't even feel.

Avoid a big tax bill

Getting a huge tax bill can ruin your day. The IRS requires that you pay 100% of the previous year's tax liability or 90% of the current year's tax bill. If you expect a change in income or a major life change, you might consider making estimated tax payments throughout the year so you don't have a big surprise coming April 15th. This can be done through a tax projection. Don't worry if you miss one quarter payment, you can still make the other quarterly estimated tax payments. The third quarter estimate is due September 15th and the fourth quarter estimate is due January 15th, so make sure to plan according.

Consider making charitable donations

Since the CARES Act was implemented in 2020, non-itemizers where allowed to deduct $300 in charitable donations from their AGI (adjusted gross income) on their tax return. For 2021, The Consolidated Appropriations Act expanded the deduction up to $600 for married filling joint return and still $300 for single fillers. Keep in mind that these must be cash donations for non-itemizers. Receipts must be kept for your records for all your non-cash and cash donations.