



FOR THE LIFE OF YOUR BUSINESS

Tax Considerations for Small Businesses

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Tiffany D. Bell
Senior Associate
Andreozzi Bluestein LLP

Important Resources:

- New York State Department of Taxation and Finance
 - www.tax.ny.gov
- Internal Revenue Service
 - www.irs.gov
- New York Department of State- Division of Corporations
 - www.dos.ny.gov
- New York State- Business Express
 - www.businessexpress.ny.gov

I have a great business idea, now what?

- Business Plan
- Name your business
- Chose a legal structure
- Obtain funding
- Must comply with federal law and the laws of any state in which you operate your business
 - What, if any, licenses are required?
 - What, if any, permits are required?
 - What, if any, registrations are required?
 - What taxes must be paid?

In this world nothing is certain but death and Taxes

For new business owners it is more like:

Nothing is scarier than death and taxes

- Don't panic
- Use your resources
- Assemble your team of professionals
- Arm yourself with knowledge and good advisors
- No matter how overwhelmed you feel do not bury your head in the sand and hope it goes away

Business Entities

- Sole Proprietorship
- Partnership
- Corporation
 - C Corp
 - S Corp
- Limited Liability Company

Which business structure is best for your business?

Which business structure is best from a tax perspective?

Sole Proprietorship

- A business owned and operated by one person.
- Simplest and most common form of small business organization
- There are no administrative requirements other than filing a DBA
- It is not a separate legal entity (the owner is personally liable for all of the debts and liabilities of the business)
- Business profits and losses are reported on the proprietor's personal income tax return
- There is only one level of taxation
- May obtain an Federal Employer Identification Number (EIN) from IRS or you can use your SSN. However, you do need an EIN if you have employees

Partnership

- A business owned by two or more persons
- Simple to form- there are only a few administrative requirements- DBA required if not using natural names
- The partnership is a separate legal entity from its owners
- The partners have unlimited personal liability for the debts of the partnership
- There is a partnership tax return due, but it is an information return, the partner's pro-rata share of the profit and losses of the partnership business are reported on the partner's personal income tax return (pass through)
- There is only one level of taxation
- Not legally required, but should have a partnership agreement
- Must obtain an Federal Employer Identification Number (EIN) from IRS

Corporations

- A separate legal entity from its owners (Shareholders)
- Shareholders have limited personal liability
- Formed by filing a Certificate of Incorporation with the New York Secretary of State (fee is about \$200 and you can file on line)
- Can have one or more owners (shareholders)
- Corporations **MUST** obtain an EIN
- There are numerous “corporate formalities” required by law
 - Must hold annual shareholder meetings
 - Must elect directors and officers annually
 - In NY: subject to affirmative requirements under the Business Corporation Law
- Corporations are by default “C Corporations” under the Internal Revenue Code
- What’s known as an S Corp, is actually an “election” a C Corporation can file to elect to be treated as a “subchapter s corporation”

C Corp Taxation vs. S Corp Taxation

- **C Corp Taxation:**
 - Taxed at the entity level (21%) – Corporation’s profits are taxed AND...
 - Taxed at the shareholder level (0%-20%)- SH’s dividends are taxed
 - Subject to State Franchise Tax
- **S Corp: To qualify to make the S Election, the corporation must**
 - Be a domestic Corporation
 - Have only allowable shareholders (essentially individual citizens or permanent residents-- no partnerships, corporations* or non-resident alien shareholders)
 - Have no more than 100 Shareholders
 - Have only one class of stock
 - Is not an “ineligible corporation” (ie. Certain financial institutions, insurance companies)
- **S Corp Taxation:**
 - Single level of taxation- gains and losses of the corporation “pass through” to the shareholder (reported on the shareholder’s personal income tax return)
 - Subject to State Franchise Tax

Limited Liability Company (LLC)

- An unincorporated organization of one or more members
- Separate legal entity
- Formed by filing Articles of Organization with New York Secretary of State (fee is \$200 and there is a Biennial Statement fee of \$9)
- Must adopt a written operating agreement
- There is a publication requirement (cost depends on where you publish)
- Each member (owner) has limited liability for the contractual or other liabilities and debts of the company
- Single Member LLCs are treated as sole proprietorships for income tax purposes
- Multi-Member LLCs are treated as partnerships
- LLCs can elect to be taxed as a corporation (and can make the S Election)

Business Taxes

- **Federal**
 - Income Tax
 - Self-Employment Tax
 - Social Security and Medicare Taxes
 - Income Tax Withholding
 - Federal Unemployment Tax (FUTA)
 - Excise Tax
- **State (New York)**
 - Income Tax
 - Corporate Tax
 - Franchise Tax
 - Sales and Use Tax
 - Withholding Tax

Every business has tax filing obligations whether or not it makes a profit

Federal Taxes- Sole Proprietorship

- **Income tax- Form 1040** Individual income tax return -DUE April 15th
- **Schedule C** (profit or loss from the business) or Schedule C-EZ
- **Self-employment tax- Schedule SE** (SSA uses this information to figure your benefits under the Social Security program)
- **Estimated taxes** for Individuals- **Form 1040-ES** (method used to pay tax on income not subject to withholding) Due April, June, Sept and January (See form instructions for details)
 - Penalties may be applied if you didn't pay enough estimated tax for the year or you didn't make the payments on time or in the required amount (penalties can be imposed even if you have an overpayment on your return)

Federal Taxes-Sole Proprietorship

- **Social security and Medicare taxes and income tax withholdings- Form 941**, Employer's Quarterly Federal Tax Return- used to report income taxes, social security tax or Medicare tax withheld from employee's paychecks and used to pay the employer's portion of social security or Medicare tax
 - DUE April 30; July 31; October 31; and January 31 (see instructions for more details)
 - Responsible for providing information on these items by providing W-2 to employees and W-3 to SSA (due annually)
 - Penalties can be imposed if you pay the taxes late and if you file the returns late, including Forms W-2 and W-3.
- **Federal unemployment tax (FUTA)- Form 940-** Employer's Annual Federal Unemployment Tax Return-used to report the annual FUTA tax. The FUTA tax provides funds for paying unemployment compensation and is paid by the employer. This is not a withholding tax. Due January 31
- **Excise Taxes-** Excise taxes are taxes paid when purchases are made on a specific good, like gasoline, or activities, like wagering or highway usage by trucks. They are usually included in the price of the product. See [irs.gov](https://www.irs.gov) for more information on goods and activities subject to excise taxes.

Federal Taxes- Partnerships

- A partnership must file an annual information return to report the income, deductions, gains, losses, etc., from its operations, but it does not pay income tax. The profit and losses of the partnership “pass through” to its partners. Each partner includes his/her share of the income or loss on his/her individual income tax return.
- Partnership returns
 - **Annual Return of Income- Form 1065-** DUE March 15
 - **Employment taxes: Forms 941 and 940**
 - **Excise Taxes**
- Partner’s returns
 - **Form 1040** (Individual Return) and **Schedule E**, Supplemental Income and Loss- used for income from rental real estate, royalties, partnerships, S corporations
 - **Schedule SE** self-employment tax
 - **Form 1040-ES**, Estimated Tax for Individuals

Federal Taxes- Corporations

- In forming corporations, shareholders contribute money and/or property for the corporation's capital stock
- A corporation generally takes the same deductions as a sole proprietorship in order to determine its taxable income
- C Corporations are separate taxpaying entities- it earns income, has expenses, pays taxes and distributes profits to shareholders
- Double Taxation- C Corporations are taxed at both the entity level (profits taxed when earned) and the shareholder level (profits taxed to the individual shareholders when distributed as dividends)
- The corporation does not get a deduction when it pays dividends to the shareholders
- Shareholders cannot deduct any loss of the corporation

Federal Taxes- C Corporations

- **Income Tax- Form 1120**, U.S. Corporation Income Tax Return- Generally due April 15th
- **Estimated Tax- Form 1120-W-** Generally corporations must make estimated tax payments if they expect their estimated tax to be \$500 or more- Due the 15th of the 4th, 6th, 9th and 12th months of the tax year
- **Employment taxes- Quarterly Forms 941** for Social Security and Medicare taxes and income tax withholding; **Annual Form 940** for FUTA Taxes
- **Excise Taxes**

Remember- Shareholders have their own personal income tax reporting obligations on dividends received from the C Corporation

Federal Taxes- S Corporations

- S corporations are corporations that elect to pass corporate income, losses, deductions, and credits through to their shareholders for federal tax purposes.
- Shareholders report the flow-through/pass through of income and losses on their personal tax returns and are assessed tax at their individual income tax rates
- No Double Taxation issues
- S Election must be made by filing Form 2553 within 2 months and 15 days after the beginning of the tax year the election is to take effect (generally March 15th)
- There are ways in which you can “blow” your S election and lose the benefit of such election, be aware of how and ensure you don’t inadvertently lose the status

Federal Taxes- S Corporation

- **Income Tax- Form 1120S-** U.S. Income Tax Return for an S Corporation -Due generally March 15th
- **Estimated Taxes- Form 1120-W-** if required due the 15th day of the 4th, 6th, 9th and 12th months of the tax years
- **Employment taxes- Quarterly Forms 941** for Social Security and Medicare taxes and income tax withholding; **Annual Form 940** for FUTA Taxes
- **Excise Taxes**
- **Shareholders-**
 - **Income Tax- Form 1040 and Schedule E** (using Schedule K-1 provided by the S-Corporation)
 - **Estimated Tax- Form 1040-ES-** if required due in April, June, September and January, see instructions for details

Federal Taxes- LLC

- IRS will treat an LLC as either a corporation, partnership or as part of the LLC's owner's tax return (a “disregarded entity”)
 - A Single Member LLC will be a disregarded entity unless it files **Form 8832** and elects to be taxed as a corporation (if it does, can also elect to be taxed as an S corporation)
 - Two (or more) Member LLC will be treated as a partnership for income tax purposes unless it files **Form 8832** and elects to be treated as a corporation (if it does, it can also elect S status)
 - Single Member- Sole proprietor – follow sole proprietor rules
 - Multi- Member- Partnership- follow partnership rules
 - LLC Elects to be treated as a corporation- follow corporation rules
 - LLC Elects to be treated as an S corporation- follow S corp rules

Potential Civil Penalties

- IRS has so many penalties, too numerous to name, but common penalties include:
- Failure to file penalties (or File late) income tax returns- 5% for each month the return is late, but not more than 25%
- Fraud penalty – 75%
- Failure to file information return penalties (or file late)- depends on the return but can range from \$200 to more than \$10,000
- Failure to pay penalties (or pay late)(Be aware that an extension to file a tax return is NOT an extension to pay late!)
 - Penalties may be assessed if the tax is not paid when due -may be assessed ½ of 1% of the unpaid tax for each month the tax isn't paid, up to a max of 25% of the unpaid tax
- Incomplete or inaccurate information returns (considered “not filed”)
- Frivolous return penalty- \$5000 (a return that doesn't contain information needed to figure the correct tax or shows a substantially incorrect tax because the taxpayer takes a frivolous position on their return)
- Trust Fund Recover Penalty-This may apply if certain excise, income, social security and Medicare taxes that are collected or withheld are not paid over. This penalty could be imposed on all persons who IRS determines are responsible for collecting, accounting for, or paying over these taxes, and who acted willfully in doing so. The penalty is equal to the full amount of the unpaid trust fund tax
- Accuracy related penalty- underpaid tax due to negligence, substantial understatement, transaction lacks economic substance, etc 20% of the underpayment or 40% if any portion of the underpayment is attributable to a undisclosed foreign asset or noneconomic substance transaction
 - Negligence penalty- failure to make a reasonable attempt to comply with the tax law or exercise ordinary and reasonable care in preparing a return or keeping adequate books and records-
 - Substantial understatement penalty- Substantial if understatement is more than the larger of 10% of the correct tax or \$5,000.

Criminal Penalties

- Tax evasion
- Willful failure to file a return, supply information or pay any tax due
- Fraud and false statements
- Preparing and filing a fraudulent return
- Identity Theft

New York State Taxes

- Income Tax
- Sales Tax
- Withholding Tax
- Corporation Tax

Due dates for NY returns can be found at:
<https://www.tax.ny.gov/help/calendar/>

Income Tax- New York State

- **Sole Proprietorship**
 - **Form IT-201: Resident Income Tax Return (for full-year NYS residents)**
 - Form IT-203: Nonresident and part-year Resident Income Tax Return
 - Form IT-2105, Estimated Income Tax Payment Voucher for Individuals (if you will owe NYS, NYC or Yonkers income tax)
- **Partnerships**
 - **Form IT-204: Partnership Return** (information return for the partnership- the partnership does not pay state income tax –Instead, the partner's share of the income is reported on the partner's personal income tax return)

New York State Taxes- Corporation

- Domestic corporation is a corporation incorporated under the laws of NY State
- Foreign corporation is a corporation incorporated under the laws of another state or foreign country. Foreign corporations must be authorized by the New York State Department of State to do business in the state.
- S- Corporation- corporations that have made and been approved for the federal election, may make a NYS election on Form CT-6. If approved by NY, SHs of the corporation will pay NYS personal income tax on their pro rata share of income earned by the S corporation
- Corporations typically file franchise tax returns on an annual basis- Form CT-3 or CT-3-S (for S corporations)

New York State Taxes- LLC

- An LLC that is treated as a partnership for federal income tax purposes will be treated as a partnership for New York tax purposes
- An LLC that is treated as a corporation, including an S corporation, for federal income tax purposes will be treated as a corporation for New York tax purposes or as a New York S corporation if the New York S Election is made
- Every partnership (including an LLC or LLP that is treated as a partnership for federal income tax purposes) that has income derived from New York sources may be required to pay estimated income tax on behalf of its partners or members who are nonresident individuals or corporations (other than NY S corporations)

See instructions for forms IT-2658; CT-2658; IT-2658-E; CT-2658-E for more information.

New York Taxes for Employers

- Unemployment insurance, wage reporting and withholding tax-
 - Form NYS-45 (Quarterly Combined Withholding, Wage Reporting, and Unemployment Insurance Return)
 - Usually filed online
 - Due April 30, July 31, October 31, and January 31
 - Penalties for late filing- can increase the longer the returns remain unfiled

New York State Sales Tax

- If your business intends to sell goods or services that are subject to sales tax, you need to get a Certificate of Authority from New York State
- The Certificate of Authority proves that you are registered for sales tax purposes
 - need to apply for 20 days before you intend to do any business that requires you to collect sales tax, or issue or accept exemption certificates
 - If your business makes taxable sales before receiving the Certificate of Authority, you may be subject to a penalty of up to \$10,000
- Sales tax returns are generally filed and paid through the Sales Tax Web File
- Quarterly filers use Form ST-100 (Due quarterly March 20th, June 20th, September 20th and December 20th) NOTE: sales tax quarters are not calendar year quarters
- Annual filers use Form ST-101 (Due March 20th)

Some Other New York Taxes

- Metropolitan Commuter Transportation Mobility Tax
- Cigarette and tobacco products tax
- Alcoholic beverage tax
- Petroleum business tax
- Highway use tax
- Fuel use tax
- Waste tire management fee
(plus about 20 more tax types)

Recordkeeping

- Businesses are expected to keep good records for all required tax and information returns
- The availability of and sufficiency of the business records will impact your success in an audit and/or in requests for penalty abatement
- Recordkeeping requirements vary depending on the taxing authority, and the type of tax or information being reported, but generally:
 - you need to keep records for a minimum of three to seven years
 - The records should accurately reflect the income and expenses you report on your returns
 - The records should be made contemporaneously
 - The records should be made available upon request of the taxing authority
 - There are penalties for not having or making available certain records

Recordkeeping- Sales Tax

- Sales Tax records must show:
 - Gross sales
 - Taxable sales
 - Purchases subject to sales or use tax
 - Sales and use taxes due for the specific locality in which the items or services were delivered to your customers
 - Other special taxes due
- Sales Records must show:
 - Every sale
 - Amount paid, charged or due on the transaction
 - The sales tax due, if any
 - Must retain receipts or copies of receipts for transactions (or keep a daily record of all cash and credit sales in a day book or journal)
 - Must be sufficiently detailed to independently determine the taxable status of each transaction and the amount of tax due and collected

Recordkeeping- Sales Tax

- **Delivery records**

- Must maintain records that substantiate points of delivery of the taxable products or services you sell if you delivered the product or service to a place other than your place of business
- Keep records of delivery such delivery receipts, parcel post receipts, bills of lading, driver log books, etc

- **Purchase records**

- Must keep detailed records of the nature, type, value, and amount of all business purchases, purchases invoices, and prepare daily, weekly or monthly analysis

Failure to keep adequate records could lead to penalties, substantial additions to tax, and suspension or revocation of your Certificate of Authority

Recordkeeping- Payroll and DOL audits

- Records must be kept in a manner that will enable IRS and NYS DTF to ascertain whether any tax liability has been incurred and, if so, the extent of the liability (Similar records are required for DOL)
 - the name, address, and Social Security number of each employee
 - the total amount and date of each payment of compensation
 - the period of service covered by each payment of compensation
 - the portion of each payment of compensation that constituted taxable wages
 - copies of each employee's withholding exemption certificate (Form W-4)
 - dates and amounts of tax deposits you made
 - copies of returns you filed
 - copies of any undeliverable Form W-2

If you hire employees:

- Must obtain an Employer Identification Number (EIN)
- Must register with New York State
- Must provide certain information about newly hired employees
- You may have to withhold NY state, NY city or Yonkers income tax from employees' pay and remit to NY Tax Department
- You may need to pay New York State Unemployment Insurance contributions
- You may need to carry workers' compensation and state disability insurance (SDI)
- You may be required to make periodic tax deposits (Federal)

In conclusion:

- Taxes can impact business decisions and business decisions can impact your tax obligations
- Keep an eye on your cashflow, especially when your business starts growing
- Dangers of not watching your cashflow
- Link between business tax liability and personal tax liability
 - Effect of delinquency on your personal circumstances- including Federal Passport revocation and NYS Driver License suspension
- As your business grows, tax issues can get more complicated. Rely on professionals but **KNOW** your business!

Important Resources:

- New York State Department of Taxation and Finance
 - www.tax.ny.gov
- Internal Revenue Service
 - www.irs.gov
- New York Department of State- Division of Corporations
 - www.dos.ny.gov
- New York State- Business Express
 - www.businessexpress.ny.gov