Tax Tips

A NEWSLETTER FOR NEW BUSINESSES

courtesy of

The Internal Revenue Service

IRS Tax Assistance Telephone Numbers

1-800-829-1040
for general tax assistance

1-800-829-4477
TeleTax
for recorded tax information

1-800-829-3676
for FREE
tax forms and publications

September 1995

PLANNING FOR THE FUTURE: IRA, Keogh and SEP Plans

Whether your retirement days are around the corner or well over the horizon, as a well-informed business person you should be up to date on the types of retirement plans available. In addition to providing for a comfortable retirement, certain plans have the distinct added advantage of offering significant tax benefits today.

The plans you will hear most about as a self-employed business owner are IRAs, Keoghs and SEPs. They all offer similar savings opportunities and tax advantages for people who run their own businesses.

Individual Retirement Arrangement (IRA): IRAs are savings plans that let you set aside money until retirement. The amounts earned by the contributions you make to an IRA are not taxed until you withdraw the money, and it is presumed at retirement you will be paying a lower tax rate than you do today. That alone makes the IRA a significant tax break for many people.

There are certain restrictions on who can qualify for an IRA. You can usually set up an IRA if you are under age 70 1/2 and have taxable compensation greater than or equal to your contribution during the year. Individuals can generally contribute up to $2,000 a year to their IRAs. This contribution may be tax deductible in full, in part or not at all. If neither you nor your spouse is covered by an employer retirement plan, the contributions will be fully deductible. If either you or your spouse is covered by an employer plan, your contributions will not be deductible unless your earned income is below certain thresholds. Generally, you cannot withdraw any of the money before you turn age 59 1/2 without being penalized and taxed.

Banks, financial institutions, mutual funds, and stockbrokers all offer a variety of IRS-approved IRA plans.

Self-employed people can participate in the following two plans even if their spouses are covered by a plan.

Keogh Plan: The theory is similar to that of an IRA. A Keogh Plan is a retirement plan where taxes can be deferred until retirement. You can generally contribute much more to a Keogh plan than

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to an IRA. If your Keogh is a "money purchase plan," your contribution can be as much as 25 percent of the employee participants' compensation. The 25-percent limit is adjusted for your own contribution deductions. If your Keogh is a "profit sharing plan," your contribution can be up to 15 percent of the compensation, but you can vary the amount contributed each year. In either plan, no more than $30,000 can be contributed for each participant. If you have employees in your business, you usually include them in your Keogh plan.

Once again, most banks and insurance companies are well-equipped to set up an IRS-approved Keogh for your business.

Simplified Employee Pension Plan (SEP): Still another retirement plan alternative is the SEP. These were specifically designed for small employers and have very few administrative burdens or costs. Your contributions (which can be up to 15 percent of the employees' compensation or $30,000) are made directly to IRAs that the employer sets up for the employees.

For a more detailed look at retirement plan options for your business, ask for the following free Publications.

- *Publication 590, Individual Retirement Arrangements (IRAs)*
- *Publication 560, Retirement Plans for the Self-Employed.*

Self-Employment Tax:

The Do-It-Yourself Social Security Program

The Social Security system, our national retirement program since 1933, is funded directly by taxpayers. FICA, the Social Security tax, and Medicare tax are deducted from virtually every pay envelope in the country, helping to provide retirement income and Medicare coverage to millions of Americans.

Self-employed taxpayers, including business owners like you, are also protected by Social Security and Medicare coverage. But you pay for your coverage through a different procedure, a tax called the Self-Employment Tax, which you must pay along with your federal income tax each year.

For the most part, if you carry on a trade or business, are not an employee and are in business for yourself, then you are self-employed. Part-time work can qualify as self employment even if it's work you do in addition to a regular full-time job. If you have net earnings from self employment of $400 or more a year, you may have to pay the self-employment tax.

In most cases, self-employment income does not include interest, dividends, capital gains or rent from real estate.

Most self-employed people will have to pay the self-employment tax throughout the year as a part of their quarterly estimated tax payments. The current rate is 15.3 percent. It's important to remember that your self-employment tax will raise the total federal tax you owe. Be sure to take this into account when you determine how much estimated tax to send in each quarter. When you file your tax return, you must fill out Schedule SE, on which you report your self-employment income and calculate the tax you owe.

For more information about who must pay self-employment tax, ask for free Publication 533, Self-Employment Tax.

Developing Good Bookkeeping Practices Today

One of the best investments of your time is setting up a bookkeeping system that will help you monitor your business and keep good records. Here are a few ideas that help make it easier.

Petty Cash: A petty cash fund may be more useful than your checking account when it comes to paying for small items. Whenever you pay for something from petty cash, make out a "petty cash slip" and attach it to the receipt as proof of payment.

Set up your petty cash fund so it always has a fixed amount assigned to it, for example, $100. The cash on hand and the receipts should always total $100. When the cash starts to run low, write a check to "Petty Cash" to bring the total back up to the $100 level. The petty cash slips can then be recorded in the appropriate categories in your monthly expense journal.

Separate Bank Accounts: Keep your personal funds completely separate from your business accounts.

Separate Business Checking Accounts: One for payroll and another for all other business expenses.

Loans: If you receive money in the form of a loan, set up a separate account for that money. Never mix loan money in with your other business receipts.

Personal Funds: If you make a loan to your business or otherwise put your own money into the business, keep very good records of the transaction. Again, don't mix these funds with your other business income, or it might be mistaken as taxable business income.

The IRS Collection Process:

When the Check Is Not in the Mail

Just like any business, when tax bills are not paid on time the IRS must take action to collect the money owed. To do otherwise would be unfair to the millions of taxpayers who pay their fair share of taxes. And, more simply, it's the job assigned to the IRS by Congress.

This is the task of the IRS Collection Division: collecting underpaid, missing or delinquent taxes.

Business owners may find themselves dealing with the Collection Division for a variety of reasons. Self-employed persons may repeatedly neglect to make quarterly estimated tax payments. Employers may fail to deposit the taxes withheld from their employees' wages, or they simply may not file their tax returns.

Regardless of the reason, the IRS is obligated to collect the money owed to the government. The collection tools available to do the job include a series of tax due notices and, finally, enforced collection actions.

Notice and Demand: The tax due notices ensure that the taxpayer knows, beyond all doubt, that the IRS believes tax money is owed, what the amount of the delinquent tax bill is, and that the IRS is serious about collecting it.

The first notice that is sent usually demands an explanation for the missing tax money or full payment within ten days. Interest and penalties are usually added to the original amount owed.

Most people settle their tax bill at this time. Of course, those who feel that the bill is wrong should, by all means, contact the IRS immediately and gather the records to support their position.

In the case of someone who owes but doesn't have the money to pay, arrangements frequently can be worked out with the IRS to make installment payments. But the IRS must know about such a problem before arrangements can be worked out.

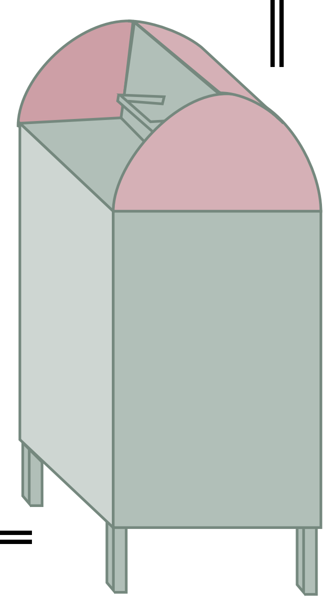
Usually, the IRS will send up to four notices before taking enforced collection measures.

Enforced Collection: This is the side of the IRS no one wants to see. Enforced collection can include a levy, which allows IRS to take property to satisfy tax debt. The property can include salaries, bank accounts, business or personal property. The IRS will issue a "Final Notice of Intent to Levy" thirty days before seizing any property.

People can usually redeem seized property before it is sold by settling their tax bill (plus interest, penalties and related seizure expenses).

There is one word of advice about the collection process that should be remembered above all others: never ignore collection notices. Doing so can be a very expensive error.

More information is available in the free IRS Publication 594, Understanding the Collection Process.



Tax Tips

Internal
Revenue
Service

PC:C:C
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Washington, DC 20224-2686

Taxcalendar

September 1

Deposit payroll tax for payments on August 26, 27, 28 and 29.

September 7

Deposit payroll tax for payments on August 30, 31 and September 1.

September 8

Deposit payroll tax for payments on September 2, 3, 4 and 5.

September 11

Deposit environmental, fuel, luxury, retail and manufacturers tax for the last 16 days of August.

September 13

Deposit payroll tax for payments on September 6, 7 and 8.

September 14

Deposit gas tax for last 16 days of August if the 14-day rule applies.

September 15

Deposit payroll tax for payments in August if the semi-weekly rule did not apply.

Deposit payroll tax for payments on September 9, 10, 11 and 12.

Individuals - use Form 1040ES for the third installment of estimated tax for 1995.

Corporations - deposit the third installment of estimated tax for 1995.

September 20

Deposit payroll tax for payments on September 13, 14 and 15.

September 22

Deposit payroll tax for payments on September 16, 17, 18 and 19.

September 25

Deposit environmental, fuel, luxury, retail and manufacturers tax for the first 15 days of September.

September 27

Deposit payroll tax for payments on September 20, 21 and 22.

Deposit gas tax for the period beginning September 16 and ending September 22.

September 29

Deposit gas tax for first 15 days of September if the 14-day rule applies.

Deposit payroll tax for payments on September 23, 24, 25 and 26.

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For more information on other excise taxes, see Publication 509, "Tax Calendars for 1995," and Publication 510, "Excise Taxes for 1995."