CONTROL YOUR CASH

Your Boss is Smart. You're the Idiot.

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You go to work every morning, earlier than you'd probably like, at an assigned time. There it is, bolded and underlined in Section IV.3 ii) of the employee handbook.

"The regularly scheduled workday is from 8:30 a.m. to 5:00 p.m. Late arrivals and unexplained absences will not be tolerated."

That's from an actual employee handbook, right next to "behavior and performance standards".

If you're an adult, and people in positions of civilian authority are subjecting you to "behavior and performance standards", the battle is already lost. If you own a dog, put the dog in charge of your house and curl up in a ball by his feet. He's clearly a higher-level vertebrate than you are.

Nothing is worth this. Yes, this ebook is ostensibly about personal finance, but understand something:

Building wealth goes hand-in-hand with controlling your own destiny. You can't grow an empire, however modest, while building someone else's. If you're an employee, half your waking life is spent contributing to your boss's mortgage payments.

But how am I going to get ahead? People who only do the minimum don't get promoted. I've seen Office Space.

"Get promoted"; that's an expression rooted in the passive voice, which means someone other than you is doing the promoting. You're playing the wrong game here. A "promotion" implies that some semi-divine being has selected you to move from one rung of the ladder to a higher one.

But there's still a ladder. Balanced against a wall, which means if you're standing on it you're just a few degrees' tilt removed from not standing on it. Until then, someone else decides how far you'll advance. Don't kid yourself: all the self-help books in the world notwithstanding, *no employee decides his own fate*. Charles de Gaulle said the graveyards are full of indispensable men. Well, the unemployment lines are full of diligent employees.

This isn't a screed against capitalism, which beats the hell out of any alternative. Capitalism is going to save you, not enslave you, and we're going to show you how.

By ***incorporating***.

Your boss already did this, most likely.[1] Despite all the conspicuous trappings of wealth that he loves to show off - the car, the house, the clothing - it's this little piece of paper

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[1] If you own your business and haven't incorporated, this ebook still applies to you. More than it does to the salaried employees who are reading it, because you're already throwing money out the window.

called a ***corporate charter*** that's the most valuable thing of all. It generates income, deflects lawsuits, limits damage, and lets him pay far less than he otherwise would in taxes. It also complicates things a little, but it's totally worth it.

I don't need more complication in my life. Thanks anyway.

Look, you already bought the e-book. Keep reading and you'll discover how:

-depending on what line of work you're in, you can almost certainly make more money and pay less in taxes. Seriously, you can do this.

-you'll get self-determination, which transcends money management and is, by every measure, the most fulfilling way to live your life. Of course, this also terrifies people.

"Liberty means responsibility. That is why most men dread it."
-George Bernard Shaw

WHAT IT IS

A **corporation,** in case no one taught you this, is an artificial person. (The word derives from the same root as "corpse". It's a body.) A corporation pays taxes, at a more favorable rate than regular people do. It can sue and be sued, the latter with less chance of wiping it out than if it were a regular person. But unlike a real person, a corporation can't die. Nor can it be told to come in on Saturday, ordered to complete a sensitivity training seminar, or get hit up for Girl Scout cookie sales.

Most people think of a corporation as a business concern with international offices and a seat on the New York Stock Exchange. That's the truth, but it's hardly the whole truth. A corporation can consist of nothing but you and your thoughts. Tens of thousands of corporations are each little more than that.

If you're going to work for yourself, you want to incorporate because it's far, far better than the alternative - registering your business with your state, city, county or whatever and operating as a *sole proprietorship* (the default setting) or a *partnership*. As to why you shouldn't register your business as a sole proprietorship or partnership, we'll start by explaining what can go wrong if you do.

If anyone competent ever taught you how to shoot a gun, you probably spent hours going over safety and all the bad things that can happen before getting to the fun, loud, tearing-stuff-up part of the program. The same presumably went for learning how to drive a car, and the same goes here for incorporating:

If you own a business, and it isn't a corporation, one financial misstep can destroy you. A disgruntled employee, customer, or passerby can sue you for literally more than you're worth. Operating as a sole proprietor just means you're registered as your business's owner, nothing more. A sole proprietorship offers you no additional legal protection should something bad happen. If anything, it's even worse than being someone else's employee. At least when you're working for The Man you can't be sued for the business's alleged defects.

A partnership is almost the same thing as a sole proprietorship, except there are more than one of you. A legal partnership agreement merely states who owns what portion of the business. Under a partnership, you can still be wiped out by a lawsuit.

A **document of incorporation**, on the other hand, goes well beyond listing who owns what. It protects you in ways that other business formations can't.

Yes, this sounds like a giant make-work project and ought to be unnecessary. You can complain about that, or you can acknowledge that it's just part of the society we live in and use that to your advantage. Remember that very few people are doing this, relative to the number working in frustrating jobs and waiting for their lives to begin (or end.)

A corporation offers *limited liability*. (We're not going to stuff you full of definitions from here on in, we promise. Just read this one. And a few more that are coming.) **Limited liability** means the owners of the corporation can't be sued for more than what they invested in it. If you put $5000 into a corporation, the absolute worst thing that can happen to you is that you lose $5000, assuming you're not committing fraud or something. Put $5000 into a sole proprietorship or partnership, have a customer sue you because the refrigerator you installed exploded[2], and you could be on the hook for God knows how much.

Plus if you're successful at whatever it is you do for a living, and your business grows, investors will be a lot more amenable to investing in a corporation rather than in some guy with a shingle and a sole proprietorship certificate.

Setting up a corporation requires nothing more than a few hundred dollars and some patience. We'll get to the methodology shortly. There are 3 different types of entities you can set up a corporation as:

1. **a C Corporation**
2. **an S Corporation**
3. **a Limited Liability Company.**

The third one isn't technically a corporation, but whatever: a tomato isn't technically a vegetable, yet it behaves the same way. We'll hit all three in detail. As for the designations "C" and "S", those just refer to particular alphabetically organized subchapters of Chapter 1 of the Internal Revenue Code.

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[2] Spontaneously combusting appliances: America's underreported scourge.

A corporation works like this: you create this fictional person, and all the profits that your business enterprise generates pass through it. The corporation is owned by shareholder(s), and those shareholders each get proportionate cuts, called *dividends*.

Every major corporation that you've heard of does this, from AT&T to Zions Bancorporation. People buy shares from the corporation, or exchange them among themselves on the open market, and at fixed intervals the shareholders of record receive *dividend* payments in the form of cash (well, in the form of checks, but you get the idea.) The company's board of directors decides how big a dividend to pay out to the owners, and even whether to halt or reduce frequency of the dividends. As an owner/shareholder, you're at the directors' mercy, unless you own enough of the company to dictate who sits on the board (or sit on it yourself.)

There's no correlation between how well a company does and what dividend it pays out, if any. Some corporations argue, quite reasonably, that it's the owners' money to do with as they wish. Other corporations maintain, equally reasonably, that as much profit as possible should go back in the business.

But if the corporation is owned solely by you and/or yours, then it's *you* who appoints the directors and determines the dividend payouts.

So if I'm in business for myself, I could funnel all the profits through a corporation, pay out the dividends to myself and whomever else I let own a part of the company, and pay lower taxes on the dividends than if they were just regular old paychecks that you'd issue to an employee?

Now you're learning.

Let's do **C corporations** first, just to tell you that you don't want to form one. C corporations are gigantic; the monoliths of American commerce. Unless you have a few billion in annual sales, this is out of your league. More to the point, C corporations don't pay taxes on regular income, but do pay them on dividends. For S corporations, it's the other way around.

Huge businesses form as C corporations because they can classify most of their profits as regular income rather than dividends (and thus reduce taxes.) For an average-sized S corporation, the opposite applies.

Forget about corporations for a second and (temporarily) get in the mindset of the average salaried employee. Unless you're an upper-echelon executive, or working for a startup with grandiose dreams, your regular salary income is subject to less fluctuation than are any dividends you might receive. In our society a salary - the most common form of income - will typically stay unchanged for a year at a time. Both employer and employee know this going in and plan around it. But dividends can vary wildly, and probably don't comprise that much of your total income anyway.

Alright, time to think like an entrepreneur again. Dividends depend on so many factors, sales revenue being a primary one, that for a major corporation it's hard to tell with much certainty what December's suitable dividend payout should be when it's only January. Not so for income.

So given the difference in tax schedules between C and S corporations, it doesn't take a rocket surgeon to figure out that if you're going to form and operate under an S corporation, you want to maximize dividend income while minimizing salary income.

This is for real. Yes, you can incorporate. Your plumbing business, your freelance cosmetology work, whatever. WARNING: Tax jargon ahead, with our apologies. We'll try to make it as conversational as possible, but there's no getting around how this stuff was devised and implemented by accountants and tax attorneys who enjoyed getting verbose for the sheer impenetrability of it.

S corporations and LLCs are *flow-through entities*, meaning that the business's income is treated as the income of the owner(s). That way you can avoid *double taxation*, the major downside of the C corporation.

Double taxation is as bad as it sounds. For instance; Walmart is a C corporation, one that turned a $104 billion profit last year. Walmart pays corporate taxes on that $104 billion, and only then pays out dividends to its shareholders. If you're a shareholder, you *then* pay capital gains tax on the dividends.

That's heinous!

Agreed. And sorry.

We don't make the rules, nor understand the logic behind almost all of them. Unfortunately, we're at the system's mercy until our elected officials wake up, eliminate all existing taxes and instead enact the Control Your Cash Diagonal Tax (basic personal deduction of $*x*, *y*% on the remainder, and the Republicans and Democrats can argue about what *x* and *y* should be until reaching a consensus.) In the meantime, the best we can do is tell you that if your business operates as an S corporation or LLC you'll avoid paying both personal income tax and corporate tax on the same proceeds.

An **S corporation** doesn't pay federal income tax, but its owners each take proportionate shares of its profits (or losses) and report those shares on their personal income tax returns. From an entrepreneur's perspective, it's the best of both worlds: limited liability and no double taxation.

If you're wondering why every large business doesn't operate as an S corporation, one reason is the ordinary income versus dividends problem, listed above. Another is that S corporations can have no more than 100 shareholders, by law. (The law considers an entire family to be one person.) Also, S corporations can only be owned by individual, legal U.S. residents - no foreigners nor corporate owners. (Corporations can own parts of other C corporations, which is a complex stratagem to reduce taxes that goes way beyond our scope.) If an S corporation takes on a 101st shareholder or a foreign one, it automatically reverts to a C corporation and its corresponding tax schedule.

Also, you can't use an S corporation just to protect your investments from being taxed at standard capital gains rates. Some enterprising if naive taxpayers decided "I'll just 'sell' my IRA and other securities to my S corporation. That way I can pay S corporation tax rates, instead of regular capital gains tax rates." You actually can do that, but only up to a point. At least 3/4 of your S corporation's income has to have been generated by the business's operations, as opposed to being generated passively by means beyond the S corporation's control. Otherwise, again, the S corporation will automatically revert to a C corporation.

Got all that? Good.

The final item on the list, an **LLC** (no one refers to it by its entire name, just the acronym) is functionally similar to an S corporation with a couple of differences.

Because an LLC isn't a corporation, there's no board of directors nor officers to elect or appoint. S corporations have to have directors and officers, which adds a level of complexity and gives you the owner more people to accommodate. Granted, many S corporation owners just name friends and family members to their boards, but why bother if you don't have to?

One big advantage to an LLC over an S corporation is that the former is easier to maintain, requiring far less paperwork. S corporations have to file separate tax returns, while if you're a sole LLC owner you just file your ordinary tax return (albeit with an additional document, Schedule C, which we'll get to.) S corporations also have to prepare formal financial statements for distribution, resolutions, minutes of any meetings, etc. An LLC doesn't have to do any of that.

If you're going to do this solo, you probably want an LLC over an S corporation. Here's why:

An LLC can have any number of members, but if it's just you, the IRS considers it a "disregarded entity". That doesn't mean you don't have to pay taxes, but it does mean that *as far as the IRS is concerned, you exist but the LLC doesn't*. Any income the LLC takes in, *you* report on your individual tax return. The advantage to forming the LLC over not doing so is that you get to deduct expenses from your tax bill, which is a huge incentive that we'll get to.

If an LLC has at least 2 owners, then the IRS considers it a partnership. Which means you might as well form an S corporation. If you're the sole owner of an LLC or an S corporation, you can deduct everything you pay for health insurance from your income, dollar for dollar.

Of course, nothing's that simple. If you want, *you can do business as an LLC, but be treated as an S corporation for tax purposes.* You have the advantages of an LLC (no board of directors to appoint, etc.), and the tax savings of an S corporation. So yes, in almost every instance, you most likely want to *do business as an LLC but file your taxes as an S corporation.*

You can't just decide you're going to this and then do it; not if you don't want to spend time in a courtroom or an auditor's office, that is. There's paperwork for the LLC-as-an-S-Corp maneuver. It's IRS Form 8832, which is a 3-page form with 4 pages of notes. Page 1 looks like this:

Form **8832**
(Rev. January 2011)
Department of the Treasury
Internal Revenue Service

Entity Classification Election

OMB No. 1545-1516

Type or Print	
Name of eligible entity making election	**Employer identification number**
Number, street, and room or suite no. If a P.O. box, see instructions.	
City or town, state, and ZIP code. If a foreign address, enter city, province or state, postal code and country. Follow the country's practice for entering the postal code.	

► Check if: ☐ Address change ☐ Late classification relief sought under Revenue Procedure 2009-41

Part I **Election Information**

1 **Type of election** (see instructions):

a ☐ Initial classification by a newly-formed entity. Skip lines 2a and 2b and go to line 3.
b ☐ Change in current classification. Go to line 2a.

2a Has the eligible entity previously filed an entity election that had an effective date within the last 60 months?

☐ **Yes.** Go to line 2b.
☐ **No.** Skip line 2b and go to line 3.

2b Was the eligible entity's prior election an initial classification election by a newly formed entity that was effective on the date of formation?

☐ **Yes.** Go to line 3.
☐ **No.** Stop here. You generally are not currently eligible to make the election (see instructions).

3 Does the eligible entity have more than one owner?

☐ **Yes.** You can elect to be classified as a partnership or an association taxable as a corporation. Skip line 4 and go to line 5.
☐ **No.** You can elect to be classified as an association taxable as a corporation or to be disregarded as a separate entity. Go to line 4.

4 If the eligible entity has only one owner, provide the following information:

a Name of owner ► ____________
b Identifying number of owner ► ____________

5 If the eligible entity is owned by one or more affiliated corporations that file a consolidated return, provide the name and employer identification number of the parent corporation:

a Name of parent corporation ► ____________
b Employer identification number ► ____________

For Paperwork Reduction Act Notice, see instructions. Cat. No. 22598R Form **8832** (Rev. 1-2011)

THE FIRST BIG ADVANTAGE, DIVIDENDS

Benjamin Graham was a renowned investor who's probably most famous for teaching Warren Buffett everything he knows. Graham referred to dividends as "the investor's secret weapon." He was talking about C corporation dividends, but his axiom goes double for S corporation/LLC investors.

Again, because this bears repeating: an S corporation's shareholders (or the members of an LLC that files taxes as an S corporation) pay taxes on regular income, not on dividends. So if you're a one-person entity, you want to minimize the former while maximizing the latter.

In practice this means spending as little of your business's income on the owners' salaries as possible. That doesn't mean impoverishing them, as we'll soon discover. The remainder of the business' income, after expenditures and deductions, stands as untaxable dividends.

If you're the business's sole employee, or one of its few employees, you decide how much you want to pay yourself (out of the business's profits, of course.)

So if my business takes in a $200,000 profit, I could pay myself $1 and enjoy $199,999 in dividends that I don't have to pay taxes on?

Only if you want to raise a giant red flag with tassels and a fringe. IRS agents may be capricious and inconsistent, but they aren't stupid. Drawing a salary of $1 means you're being blatant about attempting to game the system.

So how much should I declare as salary?

This is where talking to a tax accountant pays huge dividends, as it were. A sensible, reasonable salary depends on how much you're taking in, what the cost of living is in your area, what similar one-person entities are paying out in salaries, etc. $30,000 is still pushing it. $50,000 is somewhat more believable. Again, talk to a pro.

There's also something you need to know about called *self-employment tax*, which the IRS currently levies as 15.3% of regular income. If your LLC *doesn't* elect to pay taxes as an S corporation, you're on the hook for this tax - another reason why your LLC should pay taxes as an S corporation. If you think that 15.3% sounds unfair to the self-employed, guess what? If you're salaried, you've already been paying it for years and probably didn't even know it.

Summarizing as briefly as possible, there's something called FICA (Federal Insurance Contributions Act) tax that every salaried employee pays to cover Social Security and Medicare (in the few remaining years before they go insolvent.) FICA tax is set at 7.65%, and visibly deducted from every salaried worker's paychecks. Go check your most recent stub if you don't believe us. Each employer also pays an additional 7.65%

for each employee, but that 7.65% doesn't appear in employees' paychecks because employers remit it to the IRS before their employees ever see it.

Of each 7.65%, 6.2% goes to Social Security and the remaining 1.45% to Medicare. However, the Social Security portion is capped: once you make $106,800, you don't pay any Social Security taxes beyond that. In other words, *the more you make, the less of it you pay.* That's rare example of a *regressive* tax, which differs from most taxes. (Income taxes are by and large *progressive*: the more you make, the more of it you pay. Sales taxes are mostly *flat*: you pay the same percentage regardless of how much you're spending.)

But that 15.3% self-employment tax only applies if you do file to pay taxes as an LLC. Pay taxes as an S corporation, and you distribute profits (after salaries) as dividends, which aren't subject to self-employment tax.

Bottom line: create an LLC, elect to be treated as an S corporation, pay yourself a "reasonable" salary and distribute the balance.

However, you still have to pay state (corporate) income tax, unless you live in Nevada, South Dakota, Washington or Wyoming. In the states that do levy a tax, rates range from .26% (Ohio) to 10% (Pennsylvania. Iowa charges 12% if you make >$250,000.)

THE SECOND BIG ADVANTAGE, DEDUCTIONS

If anything separates the wage-earning employee from the independent businessperson, this is it. If you're the former, everything you spend on the mundane aspects of your job - driving to work, picking up lunch on the way to visit a client, purchasing supplies that the company doesn't reimburse you for - is less money in your pocket. Which sounds self-evident, until you realize that independent businesspeople write all this stuff off and then some.

It's not uncommon for a wage-earner to shift to independent contractor status and do business as a one-person LLC, make more money, and pay far less in taxes. Which brings us to the favorite IRS form of S corporation owners and LLC owners alike, Schedule C.

Somewhere in the 6 million pages of the Internal Revenue Code is the stipulation allowing you to deduct "ordinary and necessary" expenses. The IRS doesn't define what these are, which works to your advantage. First, it'd be impossible for the people in charge of the IRS to determine what an ordinary or necessary expense is: they'd need to define them for every conceivable business, and the resulting tax code would be even more unfathomably long than it is now. Second, the IRS has solved this problem by sort of letting each industry set its own *de facto* standards. Whatever everyone else is allowed to deduct, you can deduct. This obviously depends on the business you're in, but here are some universal examples:

1. **Car** expenses. Gas, insurance, registration, brake jobs, oil changes, tires...if your vehicle is somehow connected to your job, you can deduct some of the expenses you incur using your vehicle. You do have to pick up supplies or visit clients once in a while, don't you? Whatever you do, save your receipts for all of it.
2. **Entertainment** expenses. If you take a client or potential client to dinner, and discuss business, even if you don't actually conduct any, you can write off half of what you paid.

If you think this sounds easy to abuse, maybe it is. That's not the point. The point is that *the tax code is written to benefit independent businesspeople at the expense of wage-earning employees*.

Let that sentence sink in. For most salaried employees, it's the biggest blow to their worldview they've received since the day they figured out that Santa Claus doesn't exist. Others just shrug and accept it, which is as big an indicator as any as to which members of our society are made for self-determination and which aren't. No one complains about this aspect of the tax system too loudly, though, because a) the independent businesspeople realize that they have a good thing going and b) the wage-earners don't know any better. *The laws are written by the very people who profit the most from these loopholes.*

3. **Travel** expenses, which can include everything from the obvious (plane tickets) to the less so (tipping the bellhop).
4. **Health** expenses. Your employer isn't handling your health care coverage anymore. Well, actually your new employer is: you.

This is an aside not directly related to incorporation, but you can deduct your health insurance premia dollar-for-dollar from your corporation's income. After all, it's about the most vital of expenses there is. You'll have to shop for your own insurance, instead of letting the HR department do it, but hey, additional personal responsibility is all part of being a grownup, isn't it?

There are myriad more deductions available to the earnest independent businessperson. Take a professional course, advertise, write off a deadbeat client, pay rent, use electricity and water...you can deduct it all, under the right circumstances.

IRS.gov gives details about this, but it's best to hire a tax accountant who can give you practical advice on what you can deduct and what you shouldn't attempt to. (And write off the accountant's fee.)

Yes, we're aware that after taking your money for this ebook we've now suggested twice that you should spend even more money visiting professionals. (And we're not done yet, either.) But that's what they're there for, and most people never even get themselves in a position where they can benefit from talking to someone who does this for a living. And benefit you will: a $500 visit to a tax accountant is a fantastic investment if it reduces your tax bill by $2500.

SO WHAT TO DO WITH ALL THESE DEDUCTIONS?

As for the method, it's simple if tedious. Save every receipt you receive during the year. Go to Staples or Office Depot and buy an **expanding file folder**. You can get them for as little as $6 each. Either use the printed tabs for each month of the year, or create your own categories. (As to which categories to create, you're going to find out in about 10 more lines.) Each day, keep however many receipts you incur and put them in your wallet. Don't even think about them until you get home, at which point you place them in the appropriate file. Do this every day - after a while, it shouldn't take you more than 10 seconds - and forget about it.

Not indefinitely, though. You need to track your expenses, weekly or monthly.

Great, now you want me to be an accountant, too.

Oh, stop complaining. This is freedom at a tiny price. And it's easy. QuickBooks[3] does the work for you and is all but idiotproof. The image of the flustered pizzeria owner or fabric store founder hovering over a printing calculator or scribbling entries in a ledger book late into the night is dead. You don't need to hire a bean counter in a green eyeshade for the day-to-day stuff at this point, and you might never. QuickBooks' basic software, which is likely all you'll need at this point, costs $184. Again, an investment, not an expense.
Check that: track your expenses weekly, at least at the start, to get you into the habit of doing this. Pick a time of the week when you're not doing anything else. Wednesday nights are good.

The first think you're going to do is take the receipt for the file folder and place it in the folder itself.

Be reasonable and judicious: the junk food you bought at the 7-Eleven doesn't require a receipt.

At the end of the quarter, add up how much you've spent on travel, on health, etc. and save those numbers. They're stepping stones on your road to professional freedom.

The deductions go on the aforementioned Schedule C, a surprisingly terse (2-page) document brought to you by your friends at the IRS. Here's page 1, which lists the expenses you can deduct starting at line 8:

[3] This isn't a plug. It's a recognition of the market for business accounting software. QuickBooks has something like a 95% share.

SCHEDULE C (Form 1040)

Department of the Treasury
Internal Revenue Service (99)

Profit or Loss From Business

(Sole Proprietorship)

▶ Partnerships, joint ventures, etc., generally must file Form 1065 or 1065-B.
▶ Attach to Form 1040, 1040NR, or 1041. ▶ See Instructions for Schedule C (Form 1040).

OMB No. 1545-0074
2010
Attachment Sequence No. **09**

Name of proprietor | **Social security number (SSN)**

A Principal business or profession, including product or service (see instructions) | **B Enter code from pages C-9, 10, & 11** ▶

C Business name. If no separate business name, leave blank. | **D Employer ID number (EIN), if any**

E Business address (including suite or room no.) ▶
City, town or post office, state, and ZIP code

F Accounting method: **(1)** ☐ Cash **(2)** ☐ Accrual **(3)** ☐ Other (specify) ▶

G Did you "materially participate" in the operation of this business during 2010? If "No," see instructions for limit on losses ☐ **Yes** ☐ **No**

H If you started or acquired this business during 2010, check here . . . ▶ ☐

Part I Income

1	Gross receipts or sales. **Caution.** See instructions and check the box if: • This income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, or • You are a member of a qualified joint venture reporting only rental real estate income not subject to self-employment tax. Also see instructions for limit on losses. . . ▶ ☐	1	
2	Returns and allowances	2	
3	Subtract line 2 from line 1	3	
4	Cost of goods sold (from line 42 on page 2)	4	
5	**Gross profit.** Subtract line 4 from line 3	5	
6	Other income, including federal and state gasoline or fuel tax credit or refund (see instructions)	6	
7	**Gross income.** Add lines 5 and 6 ▶	7	

Part II Expenses. Enter expenses for business use of your home **only** on line 30.

8	Advertising	8		18	Office expense	18	
9	Car and truck expenses (see instructions)	9		19	Pension and profit-sharing plans	19	
10	Commissions and fees	10		20	Rent or lease (see instructions):		
11	Contract labor (see instructions)	11		a	Vehicles, machinery, and equipment	20a	
12	Depletion	12		b	Other business property	20b	
13	Depreciation and section 179 expense deduction (not included in Part III) (see instructions)	13		21	Repairs and maintenance	21	
				22	Supplies (not included in Part III)	22	
				23	Taxes and licenses	23	
				24	Travel, meals, and entertainment:		
				a	Travel	24a	
14	Employee benefit programs (other than on line 19)	14		b	Deductible meals and entertainment (see instructions)	24b	
15	Insurance (other than health)	15		25	Utilities	25	
16	Interest:			26	Wages (less employment credits)	26	
a	Mortgage (paid to banks, etc.)	16a		27	Other expenses (from line 48 on page 2)	27	
b	Other	16b					
17	Legal and professional services	17					

28	**Total expenses** before expenses for business use of home. Add lines 8 through 27 ▶	28	
29	Tentative profit or (loss). Subtract line 28 from line 7	29	
30	Expenses for business use of your home. Attach **Form 8829**	30	
31	**Net profit or (loss).** Subtract line 30 from line 29. • If a profit, enter on both **Form 1040, line 12,** and **Schedule SE, line 2,** or on **Form 1040NR, line 13** (if you checked the box on line 1, see instructions). Estates and trusts, enter on **Form 1041, line 3.** • If a loss, you **must** go to line 32.	31	

32 If you have a loss, check the box that describes your investment in this activity (see instructions).

• If you checked 32a, enter the loss on both **Form 1040, line 12,** and **Schedule SE, line 2,** or on **Form 1040NR, line 13** (if you checked the box on line 1, see the line 31 instructions). Estates and trusts, enter on **Form 1041, line 3.**

• If you checked 32b, you **must** attach **Form 6198.** Your loss may be limited.

32a ☐ All investment is at risk.
32b ☐ Some investment is not at risk.

For Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 11334P **Schedule C (Form 1040) 2010**

THE DISADVANTAGES

You have to file self-employment taxes quarterly, instead of annually. That's it. You can hire an accountant to do this, and deduct your accountant's fees from your income.

THE MECHANICS OF THIS

Forms! Lots of them. Deep breath.

The IRS uses the term "election", as in you have to "elect" to consider yours an S corporation (or LLC). Yes, you have to fulfill all the structural requirements regarding number of owners, etc., but you also have to fill out IRS Form 2553, a zippy little 3-page number whose first page looks like this:

Form **2553**
(Rev. December 2007)
Department of the Treasury
Internal Revenue Service

Election by a Small Business Corporation

(Under section 1362 of the Internal Revenue Code)

▶ See Parts II and III on page 3 and the separate instructions.
▶ The corporation can fax this form to the IRS (see separate instructions).

OMB No. 1545-0146

Note. This election to be an S corporation can be accepted only if all the tests are met under **Who May Elect** on page 1 of the instructions; all shareholders have signed the consent statement; an officer has signed below; and the exact name and address of the corporation and other required form information are provided.

Part I Election Information

Type or Print	Name (see instructions)	**A** Employer identification number
	Number, street, and room or suite no. (If a P.O. box, see instructions.)	**B** Date incorporated
	City or town, state, and ZIP code	**C** State of incorporation

D Check the applicable box(es) if the corporation, after applying for the EIN shown in **A** above, changed its ☐ name or ☐ address

E Election is to be effective for tax year beginning (month, day, year) (see instructions) . . . . . . ▶ ____/____/____

Caution. A corporation (entity) making the election for its first tax year in existence will usually enter the beginning date of a short tax year that begins on a date other than January 1.

F Selected tax year:

(1) ☐ Calendar year
(2) ☐ Fiscal year ending (month and day) ▶ ________________
(3) ☐ 52-53-week year ending with reference to the month of December
(4) ☐ 52-53-week year ending with reference to the month of ▶ ____________________

If box (2) or (4) is checked, complete Part II

G If more than 100 shareholders are listed for item J (see page 2), check this box if treating members of a family as one shareholder results in no more than 100 shareholders (see test 2 under **Who May Elect** in the instructions) ▶ ☐

H Name and title of officer or legal representative who the IRS may call for more information

I Telephone number of officer or legal representative
(   )

If this S corporation election is being filed with Form 1120S, I declare that I had reasonable cause for not filing Form 2553 timely, and if this election is made by an entity eligible to elect to be treated as a corporation, I declare that I also had reasonable cause for not filing an entity classification election timely. See below for my explanation of the reasons the election or elections were not made on time (see instructions).

Sign Here

Under penalties of perjury, I declare that I have examined this election, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete.

▶ **Signature of officer** | **Title** | **Date**

For Paperwork Reduction Act Notice, see separate instructions. Cat. No. 18629R Form **2553** (Rev. 12-2007)

Some overregulated states make you file a separate form to be considered an S corporation, too. You have our sympathies if you live in one of them.

HOW AND WHERE DO I SET UP MY CORPORATION?

Let's start with where. The answer is either Delaware or Nevada, depending. There's a 46-way tie for 3rd place, and then New York and California bring up the rear.

You can incorporate anywhere, not necessarily in your home state. Nor do you have to incorporate in the state in which you do most (or even any) of your business. There, another common misconception debunked.

As for why to avoid California and New York, at this point it's almost as if California is going out of its way to drive businesses elsewhere. Every S corporation registered in California has to pay a surtax of 1 1/2% of its net income, minimum $800. Meanwhile New York holds a company's 10 largest shareholders personally responsible if it goes out of business and can't pay its employees, which defeats the very purpose of incorporating.

C corporations have their own reasons for incorporating in Delaware, most of them to do with favorable court rulings, but for the rest of us the major advantages to incorporating in Delaware are that you don't have to hold formal meetings, and that you can keep your corporate records wherever you want, as opposed to in a depository in Dover.

Nevada is the second-most popular state in which to register your entity. It's rapidly gaining on Delaware, which had a 70-year head start. Nevada's closing the gap at least as far as S corporations and LLCs are concerned. A few of the advantages to incorporating in Nevada are that:

-it doesn't levy a corporate income tax;
-it has no *franchise tax*, which some states collect for no better reason than they can. Even Delaware levies a $75 franchise tax ($250 for LLCs);
-Nevada is one state that hasn't signed an *information sharing agreement* with the IRS, meaning Carson City doesn't exchange taxpayer data with Washington;
-you don't have to disclose lots of personal information;
-the owners of an S corporation are known only to God, you, them, and the clerk who processes your application if she's paying attention. Not so in other states;
-if you're forming an LLC, you don't have to give up even that much. You only need to disclose who manages the LLC, not who its owners are.

In Nevada, you also don't have to create an LLC *operating agreement*, which is a convoluted piece of paper and more busywork.
You do, however, have to write up *articles of incorporation* (or for an LLC, *articles of organization*) regardless of where you choose to file. It's just a standard document that lists the vitals for your S corporation or LLC; mailing address, managers' names,

members' names, how much money you're investing in it, etc. You can find templates for these articles online.

If your entity will have employees beyond yourself, you need to pay unemployment taxes, both federal and state. That's ostensibly to bankroll employment agencies and job-training offices. Unemployment taxes average around 6%, by our loose definition of average. We didn't add up every state's rate and divide by 50, if that's what you're thinking. Besides, it'd be impossible to do so. There are a million variables. Some states charge a higher rate for younger businesses, some charge varying rates depending on what industry your business is in, and there is a universal cap (you only pay taxes on an employee's first $7000 in wages.) The rates vary across the country. Michigan charges 10.3%, Florida, 5.4%. For the most part, family members and minors are exempt everywhere. Go to your state's tax-collecting authority's website and enter "SUTA" to determine how much you'll be on the hook for ("State Unemployment Tax Authority.")

Sounds easy. I can do this myself, right? Just fill out the appropriate forms and send them in?

No.

You need to find a business that specializes in this. Delaware, for instance, requires you to use a *registered agent* that's been authorized to transact business in Delaware. That ostensibly keeps the riff-raff out. There are thousands of these businesses across the country, and most don't have their physical offices in Delaware. Google "entity formation" and your area code.

Nevada doesn't require you to set up your entity through a registered agent. You can use CorpNet, which lets you customize incorporation forms and send them to the relevant government office quickly and painlessly. Either way, incorporating in an approved state will pay for itself long before you file your first tax return.

Registered agents don't have to be attorneys, either. In fact, do the lay community a favor and find a company that specializes in business entity formation and *isn't* a law firm. You'll still be covered, and hopefully it'll mean that some lawyer won't be able to make his yacht payment that month and will have it repossessed.

A registered agent will charge you around $500. For your trouble, they'll register you with the relevant state's particular department. Most states call it their department of state, and the division that handles incorporation is usually called "Business Services" or "Corporations" or something similar.

A good registered agent will also beseech the IRS on your behalf for a 9-digit *Employer Identification Number*. In most cases, at least as far as paying taxes goes, this will replace your Social Security Number. It's the EIN that you put on your tax return, not your SSN. It's also what you'll use to open up a business account at your bank. You or your registered agent can apply here and have an EIN almost instantly. On a personal level, one of the first things you'll notice as a corporate business owner is how infrequently you'll need to use your Social Security Number. With luck, you might even forget it.

There's one more thing you can do yourself, or have a registered agent do for you. It's pretty critical.

GETTING A BUSINESS LICENSE

Of course. You can't enjoy any of these benefits if you aren't licensed to conduct business.

With rare exceptions, the highest level of government at which you need to obtain a business license is going to be the state level. You probably don't need a federal license unless you're selling guns, nuclear reactors or imported animal products.

The U.S. has 50 states, 1 federal district, 5 incorporated territories, 3,077 counties/ Louisianan parishes/Alaskan boroughs and who knows how many cities and other municipalities, so we're not going to get into what your particular case requires. The rudiments are as follows:

Every state requires a basic business license, which usually costs $100 or so and that you can renew annually for the same price. Your county or other jurisdiction might need one too. Depending on the county or city, they might even handle the state licensing for you.

The simple, uncomplicated solution is to go to this particular page at SBA.gov, the U.S. Small Business Administration's site. It tells you what your state requires, and links to any other additional licenses that your particular realm of business might require.

One more thing: depending on what your business sells, you might have to petition your state or local government (or both) for a **sales tax permit**. It's another legal hurdle you have to clear, but a low one. Again, it's still better than working for someone else. Just to pick one city at random, in Durango, Colorado you need a sales tax permit if your business is involved in

- storage
- use
- consumption
- selling
- leasing
- delivering in the cty, including:
  - retail sales
  - telecommunication services
  - gas and electric services
  - food or drink served or furnished
  - motel and hotel accommodations.

So pretty much everything. Get to know your city or county clerk's office early, visit once or twice, talk to the appropriate people, make sure you've got every j dotted and x crossed, bring your checkbook, **get receipts**, and you should never have to deal with them directly again.

All things accounted for - filing fees, unemployment taxes if they apply, the new paperwork that is now going to be your constant companion - you're still going to come out miles ahead of your average salaried worker who can't write any business expense off and who always remains one management decision away from being out of work.

Best of luck, and best of everything beyond luck. Send your stories, questions, or comments to info@ControlYourCash.com.

Starting a business

	Date Completed	Task
☐		Choose a name
☐		Is it available in the state where you'll be incorporating? Check with its Secretary of State
☐		Incorporate
☐		Decide on entity type:
☐		S Corporation
☐		LLC
☐		Prepare corporate documents
☐		**S corporation requirements**
☐		Corporate charter or Articles of Incorporation (from CorpNet)
☐		Appoint corporate officers/directors
☐		Appoint a corporate resident agent
☐		**LLC Requirements**
☐		LLC Operating Agreement (from CorpNet)
☐		Appoint an LLC resident agent
☐		File corporate document with state of incorporation
☐		Apply to the IRS for an Employer Identification Number
☐		If you choose an LLC, file Form 2553 with the IRS to elect S Corporation treatment
☐		Look up your state business license requirements on SBA.gov
☐		Apply to the state(s) where you're doing business for a business license.
☐		Apply to any city or county where you're doing business for a business license, if necessary.
☐		**Open a business checking account. You'll need:**
☐		Filed corporate charter or LLC operating agreement
☐		Employer Identification Number
☐		Signatures of the authorized officers, per your corporate documents
☐		Buy, install and set up QuickBooks to track all income and expenses
☐		Meet with your accountant and decide on a reasonable annual salary
☐		Set up quarterly tax returns with your accountant, or learn how to do it yourself