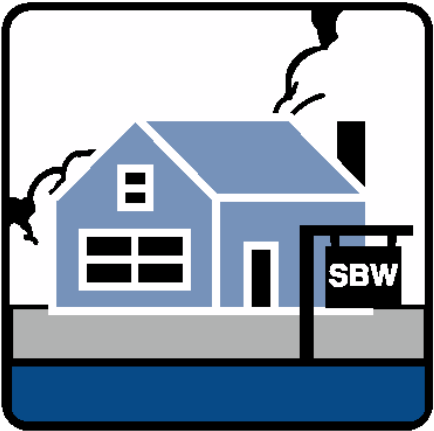


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# Small Business Tax Workshop Workbook



Department of the Treasury  
Internal Revenue Service

Publication 1066 (Rev.12-02)  
Catalog Number 46924L

[www.irs.gov](http://www.irs.gov)

# *The IRS Mission*

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

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# Small Business Tax Workshop

## Introduction

The Small Business Tax Workshop contains general information about different types of business organizations, recordkeeping requirements and business tax returns. If you need more information, see LESSON 1, pages 1-36 through 1-39, for a list of **free** Internal Revenue Service (IRS) publications. Call the IRS toll free at **1-800-TAX-FORM (1-800-829-3676)** to order.

If you have access to a personal computer, you can also download and print any of the 600 federal tax forms with instructions, approximately 100 tax publications and other tax materials from the IRS Web site at [www.irs.gov](http://www.irs.gov).

An alternative to downloading files from the Internet is Publication 1796, FEDERAL TAX PRODUCTS on CD-ROM. This CD contains over 2,000 tax materials, including prior year forms. You can purchase the CD-ROM via the Internet at [www.irs.gov/cdorders](http://www.irs.gov/cdorders) from the National Technical Information Service (NTIS) or by calling toll free **1-877-233-6767**. Fax orders are accepted at 703-605-6900. Mail orders should be sent to:

NTIS  
5285 Port Royal Rd  
Springfield, VA 22161

THE SMALL BUSINESS RESOURCE GUIDE (IRS Publication 3207) contains information important to small businesses. Order your free copy by calling **1-800-829-3676**.

Another option is to receive forms, instructions and tax information from your fax machine by calling **703-368-9694** from the phone on your fax machine and following the prompts.

There is a new section on the IRS Web site called the Small Business and Self Employed Community at [www.irs.gov](http://www.irs.gov) and **choose ‘Businesses’ from the contents menu and then ‘Small Bus/Self-Employed’**. If you run a small business or are self-employed, the site is here to help you. It offers industry profession-specific information and provides links to other helpful sites.

You will be required to pay federal employment taxes if you have employees. Lessons 2 and 3 explain your responsibilities for paying these taxes.

## Taxpayer Rights

As a taxpayer, you have the right to be treated fairly, professionally, promptly and courteously by IRS employees.

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## *IRS Mission*

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

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A discussion of your right to fairness if your return is examined or your account is in the collection process is in Publication 1, *YOUR RIGHTS AS A TAXPAYER*.

You may find it helpful to have a general understanding of some activities of the IRS and how they relate to you as a business taxpayer. There are five areas of activity within the IRS with which you should be acquainted: Customer Account Services, Submission Processing, Examination and Appeals, Collection and the Taxpayer Advocate Service.

### **Customer Account Services**

Customer Account Services is a liaison between taxpayers and IRS Submission Processing centers. Customer Account Services representatives can explain notices and answer other inquiries about your tax accounts. They can also help you understand and apply tax laws to help you determine your specific tax liability.

### **Service Centers**

Whether you electronically file or mail your business and personal tax returns, they go to a regional submission-processing center for processing. IRS processes them with an automated data processing (ADP) system. The ADP system keeps a record of all business and individual tax return transactions. Computer-generated bills for taxes due and notices explaining changes to accounts are sent to taxpayers by the submission processing centers, and submission processing centers arrange for taxpayers' refund checks to be sent to them.

### **Examination and Appeals**

The IRS is required by law to determine and collect from each taxpayer only the correct amount of tax due. One way the IRS meets this obligation is by examining returns. A notice of examination does not necessarily mean that the IRS has found, or will find, something wrong with your return.

Tax returns are selected for examination for various reasons. Returns are computer-scored according to their probability of

error. The selection may mean you did not give enough information about some item of income or deduction. You may have included nontaxable income or deducted an unallowable expense. You may have filed a claim for refund, and the return is examined to make sure the correct amount of tax is refunded.

Your tax return may be examined in your place of business, at an IRS office or at your tax representative's office. When the examination is completed, any adjustment will be explained to you. If you agree with any proposal to increase or decrease your tax liability, you will be asked to sign an agreement form. If you do not agree with any changes that are proposed by the examiner, you have certain appeal rights, both within the IRS and in the courts.

For more information, see Publication 556, EXAMINATION OF RETURNS, APPEAL RIGHTS AND CLAIMS FOR REFUND.

## Collection

Most taxpayers pay their taxes by the date the return is due. For those who do not pay on time, the collection process begins when a taxpayer is sent a notice (demand for payment) from the IRS. The taxpayer should either pay the amount due or contact the IRS immediately. If the taxpayer does contact the IRS, an IRS employee will help determine whether the notice is valid, and, if so, how to pay any amount owed.

If a taxpayer who receives a notice does not pay the amount due and does not contact the IRS, or if a taxpayer defaults on a payment agreement, the IRS may take enforcement actions. Examples of enforcement action include the filing of a NOTICE OF FEDERAL TAX LIEN, the serving of a NOTICE AND DEMAND FOR PAYMENT and/or the seizure and sale of the taxpayer's property and rights to property.

To encourage prompt payment of withheld income, social security and Medicare (employment) taxes, Congress passed a law that provides for the trust fund recovery penalty. (These taxes are called *trust fund taxes* because you actually hold the employees' money in trust until you make a federal tax deposit in that amount.) For more information, see Publications 594, THE IRS COLLECTION PROCESS and Publication 1660, COLLECTION APPEAL RIGHTS.

## Taxpayer Advocate Service

The Taxpayer Advocate is the spokesperson for taxpayers who have been unable to resolve problems through normal channels. If you have an *ongoing* tax problem, call the IRS



hotline at **1-877-777-4778** for help. You may also write to the Taxpayer Advocate at the office that last contacted you.

If the tax problem is causing or will cause you a significant hardship, the Taxpayer Advocate will arrange for an immediate review of your problem. A significant hardship may occur if you cannot maintain your business location, pay the utility bills for your business and meet payroll. Significant hardship could also occur if your business faces imminent bankruptcy or if the actions of IRS would cause irreparable damage to your business. While your account is reviewed, any additional enforcement action will be suspended if the Taxpayer Advocate determines that a significant hardship exists.

See Publication 1546, *THE TAXPAYER ADVOCATE SERVICE OF THE IRS*, for more information.

Most business taxpayers should be able to meet their tax responsibilities by using the packages of tax forms and instructions they receive from the IRS. Those who need more information may turn to the IRS' many free tax publications, education programs, audiovisual materials and other services. If additional information and assistance are needed, taxpayers can call the IRS or visit their local IRS office. By calling or visiting the IRS, taxpayers can get answers to questions about their account, general information about IRS procedures, services available or the tax law. Publication 910, *GUIDE TO FREE TAX SERVICES*, is available by calling **1-800-829-3676**.

## **Telephone Service**

Telephone tax assistance is available in all 50 states, the District of Columbia, Puerto Rico and the Virgin Islands by calling **1-800-829-1040**.

## **TELE-TAX**

Tele-Tax is an IRS telephone service that provides both automated refund information and recorded tax information. The number is **1-800-829-4477**.

## **TTY/TDD**

If you are hearing-impaired and have access to TTY/TDD equipment, you can call **1-800-829-4059** with your tax questions or to order forms and publications.



See your tax form instruction booklet for the hours of operation.

## Walk-in Service

Assistance is available in most IRS offices (Taxpayer Assistance Centers) to help you in preparing your individual federal tax return. You may also obtain tax forms, publications and help with questions about IRS notices or bills.

## Taxpayer Education Programs

The IRS has a number of programs designed to help you understand your rights and obligations under our nation's tax system. Volunteers are an important part of these programs. To volunteer to help in one of our taxpayer education programs, or for times and locations of available services in your community, call the IRS at **1-800-829-1040** and ask for the number of your closest taxpayer education office. The taxpayer education programs include:

- Community Outreach
- Volunteer Income Tax Assistance (VITA)
- Tax Counseling for the Elderly
- Small Business Tax Education
- Bank, Post Office and Library Program
- Student Tax Clinics
- Understanding Taxes Program for Students
- Practitioner Education

## Publication 17, YOUR FEDERAL INCOME TAX

This publication can help you prepare your individual tax return. It takes you through the individual tax return and explains the tax laws that cover salaries and wages, interest and dividends, rental income, gains and losses, adjustments to income (such as reimbursed employee business expenses and IRA contributions) and itemized deductions.

## IRS e-file Programs for Business

If you have employment taxes to report, you can file your Form 941, EMPLOYER'S QUARTERLY FEDERAL TAX RETURN, electronically — by telephone or through a third party such as a payroll service company. On-line filing of Form 941— through a personal computer —is also available. Visit the IRS Web site (*The Digital Daily*) at [www.irs.gov](http://www.irs.gov) for more information. In addition, you can eliminate paper deposit coupons, trips to the bank and postage costs, by taking advantage of the Electronic Federal Tax Payment System (EFTPS). This system, with millions of users, allows you to initiate your Federal Tax Deposits (FTDs) electronically by



for Business

telephone or personal computer, or you can have your financial institution initiate payments. Although this system is mandatory only for businesses that make in excess of \$200,000 in FTDs yearly, it is highly recommended and used by other smaller depositors because of its simplicity and convenience. To learn more about EFTPS or to request an enrollment form, see the website [www.eftps.gov](http://www.eftps.gov) or call EFTPS Customer Service at **1-800-555-4477**, **1-800-555-8778** or **1-800-945-8400**. See Lesson 5 for a more detailed discussion of the IRS' *e-file* Programs.

## Other Sources of Information

The following organizations offer services to people with small businesses:

- U.S. Government Printing Office – For a list of Federal publications that are for sale to assist small businesses, go to [www.gpo.gov](http://www.gpo.gov) select the 'Government Bookstore' then 'Federal Tax Products', or call 202-512-1800 (M-F, 7:30 to 5 p.m. EST). Fax orders to 202-512-2250 or write to:

Superintendent of Documents  
U.S. Government Printing Office  
P.O. Box 371954  
Pittsburgh, PA 15250-7954

- U.S. Small Business Administration (SBA) – offers many publications on topics of interest to people with small businesses. A nationwide telephone service is provided through the SBA Office of Advocacy. The U.S. Small Business Administration Answer Desk assists callers with their small business problems. It also serves as a referral service to direct callers to the appropriate government agency, trade association and other information services. The toll-free number, available Monday through Friday from 9:00 A.M. to 5:00 P.M. EST, is **1-800-827-5722**.
- Small Business Development Centers, Business Information Centers, and Women's business Centers (more than 1,000) – are available in most states and U.S. territories. Business workshops and counseling are available as well as research information for small businesses. Contact the SBA for local phone numbers and check the Internet at [www.sba.gov/sbdc](http://www.sba.gov/sbdc) for more information.
- Service Corps of Retired Executives (SCORE) and



Active Corps of Executives (ACE) – provide counseling for business people and conduct SBA-sponsored pre-business workshops. See [www.score.org](http://www.score.org).

- Social Security Administration (SSA) – The SSA provides information on proper reporting of social security wages for both paper and magnetic media filers. The SSA holds joint seminars with the IRS on proper wage reporting by employers. See [www.ssa.gov](http://www.ssa.gov) or call 1-800-772-1213/TTY at 1-800-325-0778.
- SSA and IRS issue a quarterly tax help newsletter (SSA/IRS REPORTER) which is designed to keep employers up to date on changes to their tax and employee wage obligations. View it on-line at <http://www.irs.gov>.
- National Business, Professional or Trade Organizations – provide information for specific businesses and trades. Some examples of these are:
  - National Federation of Independent Businesses (see <http://www.nfib.com/>)
  - National Association of the Self-Employed (see <http://www.nase.org/>)
  - National Association of Independent Contractors
  - U. S. Chamber of Commerce and local Chambers of Commerce (see [www.chambersofcommerce.org](http://www.chambersofcommerce.org))

National Association of Enrolled Agents (see [www.naea.org](http://www.naea.org) )

National Society of Certified Public Accountants (see [www.aicpa.org](http://www.aicpa.org))

- Other Federal Agencies provide a variety of services and information for businesspersons:
  - U.S. Department of Agriculture – The Cooperative Extension Service County Agents help rural residents manage small family businesses and farms through workshops, counseling and other types of assistance. See [www.usda.gov](http://www.usda.gov).
  - U.S. Department of Labor – The Employment Standards Administration provides assistance

regarding labor and wage relations and other labor management standards. See [www.dol.gov](http://www.dol.gov).

- U.S. Department of Commerce – The Minority Business Development Agency supports the development of minority owned and managed businesses. Commerce also has an International Business Export Office that provides information on imports and exports. See [www.doc.gov](http://www.doc.gov).
- State and Local Agencies – provide information about local laws and regulations affecting business people. Since agency and organization names vary in many states, you may want to call your local or state Chamber of Commerce for help in identifying the organization you want:
  - State Departments of Revenue, Employment, Taxation or Equalization
  - State Department of Commerce for Minority Business Development
  - State Employment Commission or Employment Security Agency
  - State Department of Economic Development for Business Regulation
  - Governor’s Office of Community and Industrial Development
  - Governor’s Office of Minority and Small Business Development
  - Small Business Development Centers and Business Resource Centers

# Lesson 1

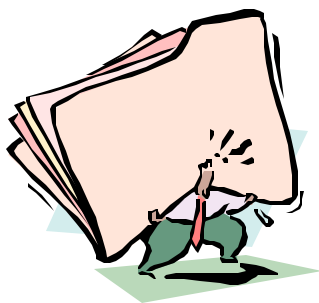
## Business Tax Requirements

**Introduction** To successfully operate your business, it is necessary to become familiar with federal, state, and local reporting requirements. This section of the workbook discusses the record keeping requirements, the advantages and disadvantages of different types of business organization, and reporting requirements for each type's federal income tax returns. Be sure to contact the state and local taxing authorities to determine their reporting requirements.

**Employer  
Identification  
Number (EIN)**  
XX -123456X

Business owners may be required to obtain a federal employer identification number to identify tax reports filed with the IRS. You may apply for an EIN by completing Form SS-4, APPLICATION FOR FEDERAL EMPLOYER IDENTIFICATION NUMBER. Afterwards, you may call, fax, or mail Form SS-4 to obtain your EIN by contacting the location that processes your state. Numbers are listed in Form SS-4's separate instructions. The application process will be discussed in more detail in Lesson 2.

**Recordkeeping** You are required to keep records so that you can prepare accurate tax returns. You must keep receipts, sales slips, invoices, bank deposit slips, canceled checks and other documents to substantiate items of income, deductions and credits. Recording these items in journals and ledgers will help you pay only the tax you owe.



Good records can help you:

- **Identify source of receipt.** You may receive cash or property from many sources. Unless you have records showing the source of your receipts, you may not be able to prove that some are non-business or nontaxable.
- **Prevent omission of deductible expenses.** You may forget expenses when you prepare your tax return, unless you record them when you incur or pay them.
- **Establish earnings for self-employment tax purposes.** Your records should show the amount of earnings reportable for self-employment tax purposes. Self-employment tax is explained later, under BUSINESS RETURNS.
- **Explain items on income tax return.** If IRS examines your

income tax return, you may be asked to explain the items reported. You must be able to support items on your return with sales slips, invoices, receipts, bank deposit slips, canceled checks and other documents. These items of support are necessary if you are to have adequate and complete records.

### Caution: Adequate Records

The record keeping rules require that you keep adequate documentary records or sufficient evidence to support your own statements, such as receipts and a log or diary, for:

- deductions you take for travel, transportation, entertainment and business gift expenses
- any deduction you take for certain business property.

These records should substantiate the amount you claim, the time and place, the business purpose and your business relationship to any other persons involved. Incomplete records may not be enough for the deduction to be allowed. If your records are lost due to circumstances beyond your control, such as by flood or earthquake, you may substantiate a deduction by reasonable reconstruction. For more information about recordkeeping, see Publication 583, *STARTING A BUSINESS AND KEEPING RECORDS*. Always keep your business records available for examination by the Internal Revenue Service.

### How Long To Keep Records

You must keep your records as long as their contents may be material in the administration of any Internal Revenue Service law.

### Supporting Records

To support items of income or deduction on your tax return, you must keep records until the statute of limitations for that return expires. Ordinarily, the statute of limitations for an income tax return expires 3

years after the return is due or filed, or 2 years from the date the tax is paid, whichever is later.



In many cases you must keep records indefinitely. For example, if you change your method of accounting, records supporting the necessary adjustments may remain material for an indefinite time.

You must keep records relating to the basis of property for as long as they are material in determining the basis of the original or replacement property. Refer to Table 3, Period of Limitation in Publication 583 for retention timeframes.

### Employment Tax Records

You must keep all employment tax records for at least 4 years after the date on which a tax return becomes due or the tax is paid, whichever is later. For more information, refer to Publication 15, EMPLOYER'S TAX GUIDE (Circular E).

### Tax Returns

Keep copies of your filed tax returns. They will help you with computing and preparing your future tax returns or if you need to correct what is on file by preparing an amended return. Previously filed tax forms may also be helpful to the executor or administrator of your estate.

### Bookkeeping Systems

Many people who operate their own, one-person, business never bother to set up a *business* bookkeeping system separate from their personal system. Their personal checking account serves as both a personal and a business account. IRS recommends that you open a separate business bank account.

You may use either a single entry or double-entry system of bookkeeping. The **single-entry system** is the simplest to keep.



With the single-entry system, you record a daily and a monthly summary of business income and a monthly summary of business expenses. Single entry is not a complete accounting system, but it shows income and expenses in sufficient detail for tax purposes. This system focuses on the business' profit and loss statement and not on its balance sheet. An example of a double-entry system is shown in Publication 583.

The **double-entry** system has built-in checks and balances and is more accurate than single-entry system. The double-entry system is self-balancing. Since all business transactions consist of an exchange of one thing for another, double-entry bookkeeping is used to show this two-fold effect.

In journals and ledgers, you record every transaction as a debit entry in one account and as a credit entry in another account. After you post the journal entries to the ledger accounts, prepare a trial balance sheet. The total debits must equal the total credits.

### Accounting Methods

On your return you must use the same accounting method you use

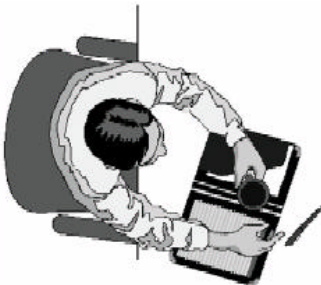
to keep your records. Your accounting method is a set of rules that you use to decide when and how you report your income and expenses.

The two most commonly used accounting methods are the cash method and the accrual method. Under the **cash method**, you report all income in the year you receive it. You usually deduct expenses only in the tax year in which you pay them. Under the **accrual method**, you report income in the year you earn it, regardless of when you receive the payment. You deduct expenses in the tax year you incur (assume liability for) them, regardless of when you pay them. If your business has an inventory, the rules have recently changed. Prior to 2000, if you had inventory, you generally had to use the accrual method for purchases and sales. Now, if your business has annual gross profits of \$1 million or less, you are permitted to use the cash method of accounting. For more information, see Publication 538, ACCOUNTING PERIODS AND METHODS.

There are several computer software packages that you can use for Record keeping. They can be purchased in many retail stores. These packages are very useful and relatively easy to use, and they require very little knowledge of bookkeeping and accounting.

*Note: If you use a computerized system, you must be able to produce sufficient legible records from the system to provide the information needed to determine your correct tax liability. Be sure to print a hard copy that matches your data on disks.*

## Income Statement and Balance Sheet



An **income statement**, also called a cash flow analysis, provides a perspective of your company's revenues, costs and profitability. A **cash flow analysis** is a detailed monthly account of how money flows into your business in the form of income and flows out of your business in the form of expenses. Subtracting expenses from income gives you a monthly result of how well your business is doing. (See Exhibit 1.1 on page 1-5.)

A **balance sheet**, on the other hand, provides a snapshot of the company's net worth at the *present* time. As the name implies, assets must balance or equal liabilities must equal net worth. (See Exhibit 1.2 on Page 1-6.)

**EXHIBIT 1.1 - CASH FLOW ANALYSIS (INCOME STATEMENT)**

QuickMart, Inc. Fortsville, TX														
Projected Direct Cash Flow (First 12 Months)														
	Start	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total
Cash on Hand	60,000	25,000	23,342	23,860	25,662	28,246	31,079	31,150	31,796	33,467	37,418	43,184	47,926	
Cash Sales		7,125	11,063	13,383	14,925	14,288	11,400	11,250	12,675	17,738	22,275	22,500	20,363	178,988
Credit Card Sales		5,000	7,500	9,000	10,000	9,500	7,500	7,500	8,500	12,000	15,000	15,000	13,500	120,000
Cash Available		<b>37,125</b>	<b>41,905</b>	<b>46,247</b>	<b>50,587</b>	<b>52,033</b>	<b>49,979</b>	<b>49,900</b>	<b>52,971</b>	<b>63,205</b>	<b>74,693</b>	<b>80,684</b>	<b>81,788</b>	298,988
Credit Card Service Charges		-150	-225	-270	-300	-285	-225	-225	-255	-360	-450	-450	-405	-3,600
Loan/Invest	140,000	0	0	0	0	0	0	0	0	0	0	0	0	140,000
<b>Total Cash Available</b>	<b>200,000</b>	<b>36,975</b>	<b>41,680</b>	<b>45,977</b>	<b>50,287</b>	<b>51,748</b>	<b>49,754</b>	<b>49,675</b>	<b>52,716</b>	<b>62,845</b>	<b>74,243</b>	<b>80,234</b>	<b>81,383</b>	
<b>Cash Paid Out</b>														
Advertising & Promotion	1,800	110	110	110	110	30	30	30	30	110	110	110	110	2,800
Bank Charges		25	25	25	25	25	25	25	25	25	25	25	25	300
Insurance		125	125	125	125	125	125	125	125	125	125	125	125	1,500
Interest		1,225	1,222	1,219	1,216	1,214	1,211	1,208	1,205	1,202	1,199	1,196	1,193	14,508
Inventory	25,000	9,055	13,007	15,502	17,203	16,776	14,743	13,917	15,287	20,305	25,838	27,136	24,084	237,873
Legal & Professional		50	50	50	50	50	50	50	50	50	50	50	50	600
Telephone		80	80	80	80	80	80	80	80	80	80	80	80	960
Payroll		1,860	1,860	1,860	1,860	1,000	1,000	1,000	1,000	2,050	2,050	2,050	2,050	19,640
Payroll Tax		60	60	60	60	60	60	60	60	124	124	124	124	2,181
Repairs & Maintenance		60	60	60	60	40	40	40	40	60	60	60	60	640
Sales Tax														0
Supplies	200	50	50	50	50	40	40	40	40	50	50	50	50	760
Taxes and Licenses		100	100	100	100	100	100	100	100	100	100	100	100	1,200
Telephone		60	60	60	60	60	60	60	60	60	60	60	60	720
Utilities		460	465	465	490	515	590	690	690	690	640	610	520	6,825
Miscellaneous		50	50	50	50	50	50	50	50	50	50	50	50	600
Subtotal	27,000	13,310	17,495	19,987	21,710	20,335	18,268	17,539	18,906	25,081	30,711	31,956	28,811	291,107
Capital Purchases	136,000													136,000
Other Organizational Costs	7,000													7,000
Deposits	5,000													5,000
Principal Payment		323	325	328	331	334	337	340	343	346	349	352	355	4,063
Owner's Withdrawal(Sole Prop or Partnership)														
<b>TOTAL CASH PAID OUT</b>	<b>175,000</b>	<b>13,633</b>	<b>17,820</b>	<b>20,315</b>	<b>22,041</b>	<b>20,669</b>	<b>18,605</b>	<b>17,879</b>	<b>19,249</b>	<b>25,427</b>	<b>31,060</b>	<b>32,308</b>	<b>29,166</b>	
<b>CASH POSITION</b>	<b>25,000</b>	<b>23,342</b>	<b>23,860</b>	<b>25,662</b>	<b>28,246</b>	<b>31,079</b>	<b>31,150</b>	<b>31,796</b>	<b>33,467</b>	<b>37,418</b>	<b>43,184</b>	<b>47,926</b>	<b>52,218</b>	







## Types of Business Organizations

One of the major considerations that must be made when deciding to go into business or after you have operated for a short length of time is the structure of ownership. So let's review the advantages and disadvantages of the five types of business organizations as well as the federal tax forms that must be filed to report their income. The five types of business organizations are: Sole proprietors, partnerships, limited liability companies, corporations and S-corporations.

### Sole Proprietorship

A sole proprietorship is an unincorporated business that one individual owns. It is the simplest type of business organization. The business does not exist apart from the proprietor (owner). The proprietor assumes the risks of the business to the extent of all of his or her assets, whether or not the assets are used in the business. If both husband and wife jointly own and operate the business, a partnership exists.

#### **Advantages:**

1. The business is simple to organize.
2. The owner has maximum freedom to make decisions.
3. The business has a minimum of legal restrictions.
4. The owner receives all the profits.
5. The business is easy to discontinue.

#### **Disadvantages:**

1. The owner has unlimited liability. The individual owner is legally liable for all debts of the business. Creditors may attach all of the entire owner's assets, even personal assets not used in the business.
2. Usually the ability to finance the business (capital) is limited to whatever the owner can secure or produce personally. This feature may limit the expansion of a business when new capital is required. A common cause of failure for this form of business organization is its original lack of capital. Limited capital restricts the ability of a sole proprietor to operate the business effectively and survive at an initial low profit level, or to get through an economic rough spot. For more information

about sole proprietorships, see Publication 334, Tax Guide for SMALL BUSINESS.

**Sole Proprietors  
(and Some Single  
Member LLCs)  
File Schedule C**

A sole proprietor (single owner) and a single member of a Limited Liability Company, LLC, file either Schedule C-EZ or C, NET PROFIT FROM BUSINESS, with their Form 1040 to report the profit or loss from operating their businesses. Exhibit 1.3 and 1.4 are examples of Schedule C-EZ and Schedule SE, Self-Employment Tax. A Schedule SE, SELF-EMPLOYMENT TAX, must be filed to report the Social Security and Medicare Taxes on net profits of \$400 or more. Self-employment tax is covered later in this lesson. A filled-in Schedule C example is shown on Exhibits 1.10 and 1.11.

**Exhibit 1.3 Sole Proprietorship – Schedule C-EZ and Schedule SE**

<p><b>SCHEDULE C-EZ (Form 1040)</b></p> <p><small>Department of the Treasury Internal Revenue Service (99)</small></p>	<p><b>Net Profit From Business</b> (Sole Proprietorship)</p> <p>▶ Partnerships, joint ventures, etc., must file Form 1065 or 1065-B. ▶ Attach to Form 1040 or 1041. ▶ See instructions on back.</p>	<p><small>CMB No. 1545-0074</small></p> <p style="font-size: 2em;"><b>2002</b></p> <p><small>Attachment Sequence No. <b>09A</b></small></p>
<p>Name of proprietor <b>Stanley Price</b></p>		<p>Social security number (SSN) <b>000 00 0000</b></p>

**Part I General Information**

**You May Use Schedule C-EZ Instead of Schedule C Only If You:**

- Had business expenses of \$2,500 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not have a net loss from your business.
- Had only one business as a sole proprietor.

**And You:**

- Had no employees during the year.
- Are not required to file **Form 4562**, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, on page C-4 to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

<p><b>A</b> Principal business or profession, including product or service <b>Barber Shop</b></p>	<p><b>B</b> Enter code from pages C-7, 8, &amp; 9 ▶ <b>8 1 2 1 1 1</b></p>
<p><b>C</b> Business name. If no separate business name, leave blank. <b>Stan's Barber Shop</b></p>	<p><b>D</b> Employer ID number (EIN), if any</p>
<p><b>E</b> Business address (including suite or room no.). Address not required if same as on Form 1040, page 1. <b>1001 Maple Ave.</b> City, town or post office, state, and ZIP code <b>Anytown, TX 70000</b></p>	

**Part II Figure Your Net Profit**

<p><b>1</b> Gross receipts. <b>Caution.</b> If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see <b>Statutory Employees</b> in the instructions for Schedule C, line 1, on page C-3 and check here <input type="checkbox"/></p>	1	27,000	00
<p><b>2</b> Total expenses (see instructions). If more than \$2,500, you <b>must</b> use Schedule C</p>	2	2,330	00
<p><b>3</b> Net profit. Subtract line 2 from line 1. If less than zero, you <b>must</b> use Schedule C. Enter on <b>Form 1040, line 12</b>, and also on <b>Schedule SE, line 2</b>. (Statutory employees <b>do not</b> report this amount on Schedule SE, line 2. Estates and trusts, enter on Form 1041, line 3.)</p>	3	24,670	00

**Part III Information on Your Vehicle.** Complete this part **only** if you are claiming car or truck expenses on line 2.

- 4 When did you place your vehicle in service for business purposes? (month, day, year) ▶ ...../...../.....
- 5 Of the total number of miles you drove your vehicle during 2002, enter the number of miles you used your vehicle for:
  - a Business .....
  - b Commuting .....
  - c Other .....
- 6 Do you (or your spouse) have another vehicle available for personal use?  Yes  No
- 7 Was your vehicle available for personal use during off-duty hours?  Yes  No
- 8a Do you have evidence to support your deduction?  Yes  No
  - b If "Yes," is the evidence written?  Yes  No

**Exhibit 1.4 Sole Proprietorship – Schedule C and Schedule SE Pub 334 pages 41-43**

<p><b>SCHEDULE SE</b> <b>(Form 1040)</b></p> <p><small>Department of the Treasury Internal Revenue Service (99)</small></p>	<p><b>Self-Employment Tax</b></p> <p>▶ <b>Attach to Form 1040.</b> ▶ <b>See Instructions for Schedule SE (Form 1040).</b></p>	<p><small>OMB No. 1545-0074</small></p> <p style="font-size: 2em; font-weight: bold;">2002</p> <p><small>Attachment Sequence No. 17</small></p>
<p>Name of person with <b>self-employment</b> income (as shown on Form 1040) <b>Stanley Price</b></p>		<p>Social security number of person with <b>self-employment</b> income ▶ <b>000 00 0000</b></p>

**Who Must File Schedule SE**

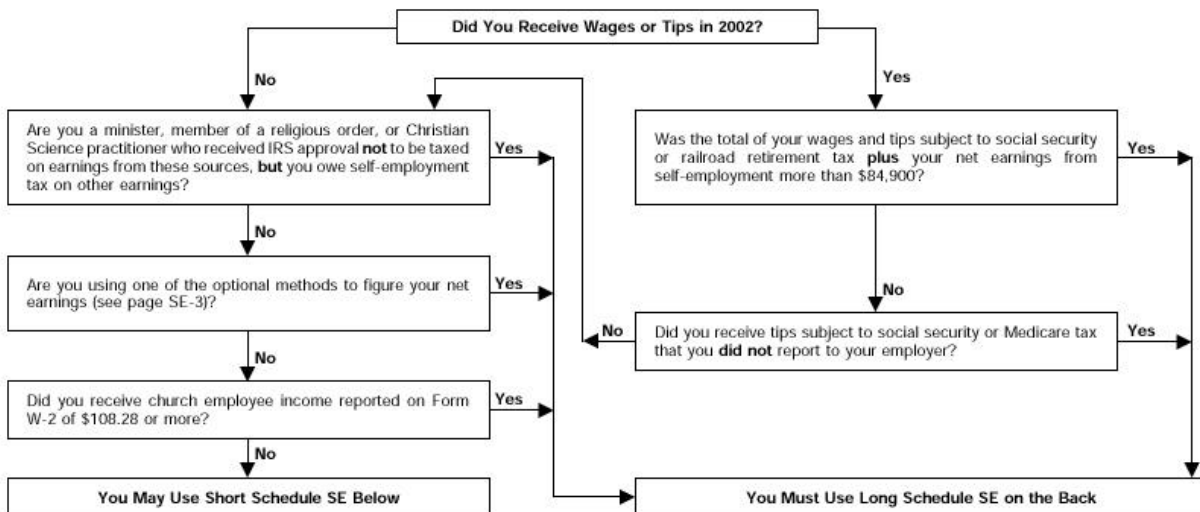
You must file Schedule SE if:

- You had net earnings from self-employment from **other than** church employee income (line 4 of Short Schedule SE or line 4c of Long Schedule SE) of \$400 or more **or**
- You had church employee income of \$108.28 or more. Income from services you performed as a minister or a member of a religious order **is not** church employee income. See page SE-1.

**Note.** Even if you had a loss or a small amount of income from self-employment, it may be to your benefit to file Schedule SE and use either "optional method" in Part II of Long Schedule SE. See page SE-3.

**Exception.** If your only self-employment income was from earnings as a minister, member of a religious order, or Christian Science practitioner **and** you filed Form 4361 and received IRS approval not to be taxed on those earnings, **do not** file Schedule SE. Instead, write "Exempt-Form 4361" on Form 1040, line 56.

**May I Use Short Schedule SE or Must I Use Long Schedule SE?**



**Section A—Short Schedule SE. Caution.** Read above to see if you can use Short Schedule SE.

<b>1</b> Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), line 15a	<b>1</b>		
<b>2</b> Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), line 15a (other than farming); and Schedule K-1 (Form 1065-B), box 9. Ministers and members of religious orders, see page SE-1 for amounts to report on this line. See page SE-2 for other income to report	<b>2</b>	24,670	00
<b>3</b> Combine lines 1 and 2	<b>3</b>	24,670	00
<b>4</b> <b>Net earnings from self-employment.</b> Multiply line 3 by 92.35% (.9235). If less than \$400, do not file this schedule; you do not owe self-employment tax ▶	<b>4</b>	22,783	00
<b>5</b> <b>Self-employment tax.</b> If the amount on line 4 is: <ul style="list-style-type: none"> <li>• \$84,900 or less, multiply line 4 by 15.3% (.153). Enter the result here and on <b>Form 1040, line 56.</b></li> <li>• More than \$84,900, multiply line 4 by 2.9% (.029). Then, add \$10,527.60 to the result. Enter the total here and on <b>Form 1040, line 56.</b></li> </ul>	<b>5</b>	3,486	
<b>6</b> <b>Deduction for one-half of self-employment tax.</b> Multiply line 5 by 50% (.5). Enter the result here and on <b>Form 1040, line 29</b>	<b>6</b>	1,743	00

## Partnership

A partnership is a relationship between two or more persons who join together to carry on a trade or business. Each person contributes money, property, labor or skills, and each expects to share in the profits and losses of the business. Any number of persons may join in a partnership.



For the purpose of income taxes, a partnership includes a syndicate, group, pool, joint venture or other unincorporated organization that carries on a business and that is not classified as a trust, estate or corporation.

### **Advantages:**

1. It is easy to organize.
2. It may have greater financial strength than a sole proprietorship.
3. It combines managerial skills and judgments of the partners.
4. It has a definite legal status.
5. Each partner has a personal interest in the business.

### **Disadvantages:**

1. The liability of the partners is usually unlimited. Each partner may be held liable for all the debts of the business. Therefore, if one partner does not exercise good judgment, that partner can cause not only the loss of the partnership's assets, but also the loss of the other partners' personal assets.
2. The authority for decisions is divided.

### Partnerships (and LLCs Taxed as Partnerships) File Form 1065

Profits or losses from operations are reported by Partnership's (and LLCs taxed as partnerships) on Form 1065, U.S. PARTNERSHIP RETURN OF INCOME, an information return that summarizes the business activity of the partnership. The partnership gives each partner a Schedule K-1 (Form 1065), PARTNER'S SHARE OF INCOME, CREDITS, DEDUCTIONS, ETC. Then each partner uses their Schedule K-1 to complete Part II of Schedule E (Form 1040), SUPPLEMENTAL INCOME AND LOSS, and any other forms

and schedules the partner must file with his or her individual return. A sample Form 1065 is shown in Publication 541. Exhibits 1.5 through 1.7 are an example of a Schedule K-1 and Schedules E. For more information about partnerships, see Publication 541, the Instructions to Forms 1065, Partnership Income Tax Return and the Form 1040 Instructions for Schedule E.

EXHIBIT 1.5 -SCHEDULE K-1 (FORM 1065), PAGE 1

<p><b>SCHEDULE K-1</b> <b>(Form 1065)</b> <small>Department of the Treasury Internal Revenue Service</small></p>	<p><b>Partner's Share of Income, Credits, Deductions, etc.</b> ▶ See separate instructions. For calendar year 2001 or tax year beginning , 2001, and ending , 20</p>	<p>OMB No. 1545-0099 <b>2001</b></p>																																																																			
<p><b>Partner's identifying number ▶</b> _____</p> <p>Partner's name, address, and ZIP code _____</p>		<p><b>Partnership's identifying number ▶</b> _____</p> <p>Partnership's name, address, and ZIP code _____</p>																																																																			
<p><b>A</b> This partner is a <input type="checkbox"/> general partner <input type="checkbox"/> limited partner <input type="checkbox"/> limited liability company member</p> <p><b>B</b> What type of entity is this partner? ▶ _____</p> <p><b>C</b> Is this partner a <input type="checkbox"/> domestic or a <input type="checkbox"/> foreign partner?</p>		<p><b>F</b> Partner's share of liabilities (see instructions):</p> <p>Nonrecourse . . . . . \$ _____</p> <p>Qualified nonrecourse financing . . . . . \$ _____</p> <p>Other . . . . . \$ _____</p>																																																																			
<p><b>D</b> Enter partner's percentage of:</p> <table style="width:100%; border-collapse: collapse;"> <tr> <td style="width:50%;"></td> <td style="text-align: center;"><small>(i) Before change or termination</small></td> <td style="text-align: center;"><small>(ii) End of year</small></td> </tr> <tr> <td>Profit sharing . . . . .</td> <td style="text-align: center;">%</td> <td style="text-align: center;">%</td> </tr> <tr> <td>Loss sharing . . . . .</td> <td style="text-align: center;">%</td> <td style="text-align: center;">%</td> </tr> <tr> <td>Ownership of capital . . . . .</td> <td style="text-align: center;">%</td> <td style="text-align: center;">%</td> </tr> </table>			<small>(i) Before change or termination</small>	<small>(ii) End of year</small>	Profit sharing . . . . .	%	%	Loss sharing . . . . .	%	%	Ownership of capital . . . . .	%	%	<p><b>G</b> Tax shelter registration number . ▶ _____</p> <p><b>H</b> Check here if this partnership is a publicly traded partnership as defined in section 469(k)(2) . . . . . <input type="checkbox"/></p> <p><b>I</b> Check applicable boxes: <b>(1)</b> <input type="checkbox"/> Final K-1 <b>(2)</b> <input type="checkbox"/> Amended K-1</p>																																																							
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A, line 15 or 16</td> </tr> <tr> <td><b>9</b> Section 179 expense deduction . . . . .</td> <td style="text-align: center;"><b>9</b></td> <td rowspan="3">} See pages 7 and 8 of Partner's Instructions for Schedule K-1 (Form 1065).</td> </tr> <tr> <td><b>10</b> Deductions related to portfolio income (attach schedule) . . . . .</td> <td style="text-align: center;"><b>10</b></td> </tr> <tr> <td><b>11</b> Other deductions (attach schedule) . . . . .</td> <td style="text-align: center;"><b>11</b></td> </tr> <tr> <td rowspan="6" style="text-align: center; vertical-align: middle;"><b>Credits</b></td> <td><b>12a</b> Low-income housing credit:</td> <td style="text-align: center;"><b>12a</b></td> <td rowspan="2">} Form 8586, line 5</td> </tr> <tr> <td><b>(1)</b> From section 42(j)(5) partnerships . . . . .</td> <td style="text-align: center;"><b>12a(1)</b></td> </tr> <tr> <td><b>(2)</b> Other than on line 12a(1) . . . . .</td> <td style="text-align: center;"><b>12a(2)</b></td> </tr> <tr> <td><b>b</b> Qualified rehabilitation expenditures related to rental real estate activities . . . . .</td> <td style="text-align: center;"><b>12b</b></td> <td rowspan="4">} See page 8 of Partner's Instructions for Schedule K-1 (Form 1065).</td> </tr> <tr> <td><b>c</b> Credits (other than credits shown on lines 12a and 12b) related to rental real estate activities . . . . .</td> <td style="text-align: center;"><b>12c</b></td> </tr> <tr> <td><b>d</b> Credits related to other rental activities . . . . .</td> <td style="text-align: center;"><b>12d</b></td> </tr> <tr> <td><b>13</b> Other credits . . . . .</td> <td style="text-align: center;"><b>13</b></td> </tr> </tbody> </table>			(a) Distributive share item	(b) Amount	(c) 1040 filers enter the amount in column (b) on:	<b>1</b> Ordinary income (loss) from trade or business activities . . . . .	<b>1</b>	} See page 6 of Partner's Instructions for Schedule K-1 (Form 1065).	<b>2</b> Net income (loss) from rental real estate activities . . . . .	<b>2</b>	<b>3</b> Net income (loss) from other rental activities . . . . .	<b>3</b>	<b>4</b> Portfolio income (loss):	<b>4</b>	} See page 6 of Partner's Instructions for Schedule K-1 (Form 1065).	<b>a</b> Interest . . . . .	<b>4a</b>	<b>b</b> Ordinary dividends . . . . .	<b>4b</b>	<b>c</b> Royalties . . . . .	<b>4c</b>	<b>d</b> Net short-term capital gain (loss) . . . . .	<b>4d</b>	<b>e (1)</b> Net long-term capital gain (loss) . . . . .	<b>4e(1)</b>	<b>(2)</b> 28% rate gain (loss) . . . . .	<b>4e(2)</b>	<b>(3)</b> Qualified 5-year gain . . . . .	<b>4e(3)</b>	Line 4 of worksheet for Sch. D, line 29	<b>f</b> Other portfolio income (loss) (attach schedule) . . . . .	<b>4f</b>	Enter on applicable line of your return.	<b>5</b> Guaranteed payments to partner . . . . .	<b>5</b>	} See page 6 of Partner's Instructions for Schedule K-1 (Form 1065).	<b>6</b> Net section 1231 gain (loss) (other than due to casualty or theft)	<b>6</b>	<b>7</b> Other income (loss) (attach schedule) . . . . .	<b>7</b>	Enter on applicable line of your return.	<b>Deductions</b>	<b>8</b> Charitable contributions (see instructions) (attach schedule) . . . . .	<b>8</b>	Sch. A, line 15 or 16	<b>9</b> Section 179 expense deduction . . . . .	<b>9</b>	} See pages 7 and 8 of Partner's Instructions for Schedule K-1 (Form 1065).	<b>10</b> Deductions related to portfolio income (attach schedule) . . . . .	<b>10</b>	<b>11</b> Other deductions (attach schedule) . . . . .	<b>11</b>	<b>Credits</b>	<b>12a</b> Low-income housing credit:	<b>12a</b>	} Form 8586, line 5	<b>(1)</b> From section 42(j)(5) partnerships . . . . .	<b>12a(1)</b>	<b>(2)</b> Other than on line 12a(1) . . . . .	<b>12a(2)</b>	<b>b</b> Qualified rehabilitation expenditures related to rental real estate activities . . . . .	<b>12b</b>	} See page 8 of Partner's Instructions for Schedule K-1 (Form 1065).	<b>c</b> Credits (other than credits shown on lines 12a and 12b) related to rental real estate activities . . . . .	<b>12c</b>	<b>d</b> Credits related to other rental activities . . . . .	<b>12d</b>	<b>13</b> Other credits . . . . .	<b>13</b>
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<p>For Paperwork Reduction Act Notice, see Instructions for Form 1065. <span style="float: right;">Cat. No. 11394R <b>Schedule K-1 (Form 1065) 2001</b></span></p>																																																																					



**EXHIBIT 1.6 - SCHEDULE K-1 (FORM 1065), PAGE 2**

		(a) Distributive share item	(b) Amount	(c) 1040 filers enter the amount in column (b) on:
<b>Investment Interest</b>	<b>14a</b>	Interest expense on investment debts . . . . .	<b>14a</b>	Form 4952, line 1 See page 9 of Partner's Instructions for Schedule K-1 (Form 1065).
	<b>b (1)</b>	Investment income included on lines 4a, 4b, 4c, and 4f . . . . .	<b>14b(1)</b>	
	<b>(2)</b>	Investment expenses included on line 10 . . . . .	<b>14b(2)</b>	
<b>Self-employment</b>	<b>15a</b>	Net earnings (loss) from self-employment . . . . .	<b>15a</b>	Sch. SE, Section A or B See page 9 of Partner's Instructions for Schedule K-1 (Form 1065).
	<b>b</b>	Gross farming or fishing income . . . . .	<b>15b</b>	
	<b>c</b>	Gross nonfarm income . . . . .	<b>15c</b>	
<b>Adjustments and Tax Preference Items</b>	<b>16a</b>	Depreciation adjustment on property placed in service after 1986 . . . . .	<b>16a</b>	See page 9 of Partner's Instructions for Schedule K-1 (Form 1065) and Instructions for Form 6251.
	<b>b</b>	Adjusted gain or loss . . . . .	<b>16b</b>	
	<b>c</b>	Depletion (other than oil and gas) . . . . .	<b>16c</b>	
	<b>d (1)</b>	Gross income from oil, gas, and geothermal properties . . . . .	<b>16d(1)</b>	
	<b>(2)</b>	Deductions allocable to oil, gas, and geothermal properties . . . . .	<b>16d(2)</b>	
	<b>e</b>	Other adjustments and tax preference items (attach schedule) . . . . .	<b>16e</b>	
<b>Foreign Taxes</b>	<b>17a</b>	Name of foreign country or U.S. possession ▶ . . . . .		Form 1116, Part I
	<b>b</b>	Gross income from all sources . . . . .	<b>17b</b>	
	<b>c</b>	Gross income sourced at partner level . . . . .	<b>17c</b>	
	<b>d</b>	Foreign gross income sourced at partnership level:		
	<b>(1)</b>	Passive . . . . .	<b>17d(1)</b>	
	<b>(2)</b>	Listed categories (attach schedule) . . . . .	<b>17d(2)</b>	
	<b>(3)</b>	General limitation . . . . .	<b>17d(3)</b>	
	<b>e</b>	Deductions allocated and apportioned at partner level:		
	<b>(1)</b>	Interest expense . . . . .	<b>17e(1)</b>	
	<b>(2)</b>	Other . . . . .	<b>17e(2)</b>	
<b>f</b>	Deductions allocated and apportioned at partnership level to foreign source income:			
<b>(1)</b>	Passive . . . . .	<b>17f(1)</b>		
<b>(2)</b>	Listed categories (attach schedule) . . . . .	<b>17f(2)</b>		
<b>(3)</b>	General limitation . . . . .	<b>17f(3)</b>		
	<b>g</b>	Total foreign taxes (check one): <input type="checkbox"/> Paid <input type="checkbox"/> Accrued . . . . .	<b>17g</b>	Form 1116, Part II Form 1116, line 12
	<b>h</b>	Reduction in taxes available for credit (attach schedule) . . . . .	<b>17h</b>	
<b>Other</b>	<b>18</b>	Section 59(e)(2) expenditures: <b>a</b> Type ▶ . . . . .		See page 9 of Partner's Instructions for Schedule K-1 (Form 1065).
	<b>b</b>	Amount . . . . .	<b>18b</b>	
	<b>19</b>	Tax-exempt interest income . . . . .	<b>19</b>	Form 1040, line 8b
	<b>20</b>	Other tax-exempt income . . . . .	<b>20</b>	See pages 9 and 10 of Partner's Instructions for Schedule K-1 (Form 1065).
	<b>21</b>	Nondeductible expenses . . . . .	<b>21</b>	
	<b>22</b>	Distributions of money (cash and marketable securities) . . . . .	<b>22</b>	
	<b>23</b>	Distributions of property other than money . . . . .	<b>23</b>	
	<b>24</b>	Recapture of low-income housing credit:		Form 8611, line 8
<b>a</b>	From section 42(j)(5) partnerships . . . . .	<b>24a</b>		
<b>b</b>	Other than on line 24a . . . . .	<b>24b</b>		
<b>Supplemental Information</b>	<b>25</b>	Supplemental information required to be reported separately to each partner (attach additional schedules if more space is needed): ..... ..... ..... ..... ..... ..... .....		





**EXHIBIT 1.7 - Schedule E**

**SCHEDULE E  
(Form 1040)**

Department of the Treasury  
Internal Revenue Service (99)

**Supplemental Income and Loss**

(From rental real estate, royalties, partnerships,  
S corporations, estates, trusts, REMICs, etc.)

▶ Attach to Form 1040 or Form 1041. ▶ See Instructions for Schedule E (Form 1040).

OMB No. 1545-0074

**2002**

Attachment  
Sequence No. **13**

Name(s) shown on return

Your social security number

**Part I** **Income or Loss From Rental Real Estate and Royalties** Note. If you are in the business of renting personal property, use Schedule C or C-EZ (see page E-3). Report farm rental income or loss from Form 4835 on page 2, line 39.

<b>1</b> Show the kind and location of each rental real estate property:	<b>2</b> For each rental real estate property listed on line 1, did you or your family use it during the tax year for personal purposes for more than the greater of: • 14 days or • 10% of the total days rented at fair rental value? (See page E-3.)	<b>Yes</b>	<b>No</b>
<b>A</b> .....		<b>A</b>	
<b>B</b> .....		<b>B</b>	
<b>C</b> .....		<b>C</b>	

	Properties			Totals
	A	B	C	(Add columns A, B, and C.)
<b>3</b> Rents received . . . . .	<b>3</b>			<b>3</b>
<b>4</b> Royalties received . . . . .	<b>4</b>			<b>4</b>
<b>Expenses:</b>				
<b>5</b> Advertising . . . . .	<b>5</b>			
<b>6</b> Auto and travel (see page E-4) . . . . .	<b>6</b>			
<b>7</b> Cleaning and maintenance . . . . .	<b>7</b>			
<b>8</b> Commissions . . . . .	<b>8</b>			
<b>9</b> Insurance . . . . .	<b>9</b>			
<b>10</b> Legal and other professional fees . . . . .	<b>10</b>			
<b>11</b> Management fees . . . . .	<b>11</b>			
<b>12</b> Mortgage interest paid to banks, etc. (see page E-4) . . . . .	<b>12</b>			<b>12</b>
<b>13</b> Other interest . . . . .	<b>13</b>			
<b>14</b> Repairs . . . . .	<b>14</b>			
<b>15</b> Supplies . . . . .	<b>15</b>			
<b>16</b> Taxes . . . . .	<b>16</b>			
<b>17</b> Utilities . . . . .	<b>17</b>			
<b>18</b> Other (list) ▶ .....	<b>18</b>			
.....				
.....				
<b>19</b> Add lines 5 through 18 . . . . .	<b>19</b>			<b>19</b>
<b>20</b> Depreciation expense or depletion (see page E-4) . . . . .	<b>20</b>			<b>20</b>
<b>21</b> Total expenses. Add lines 19 and 20 . . . . .	<b>21</b>			
<b>22</b> Income or (loss) from rental real estate or royalty properties. Subtract line 21 from line 3 (rents) or line 4 (royalties). If the result is a (loss), see page E-5 to find out if you must file Form 6198 . . . . .	<b>22</b>			
<b>23</b> Deductible rental real estate loss. <b>Caution.</b> Your rental real estate loss on line 22 may be limited. See page E-5 to find out if you must file Form 8582. Real estate professionals must complete line 42 on page 2 . . . . .	<b>23</b>	( )	( )	( )
<b>24</b> <b>Income.</b> Add positive amounts shown on line 22. <b>Do not</b> include any losses . . . . .	<b>24</b>			
<b>25</b> <b>Losses.</b> Add royalty losses from line 22 and rental real estate losses from line 23. Enter total losses here . . . . .	<b>25</b>	( )	( )	( )
<b>26</b> <b>Total rental real estate and royalty income or (loss).</b> Combine lines 24 and 25. Enter the result here. If Parts II, III, IV, and line 39 on page 2 do not apply to you, also enter this amount on Form 1040, line 17. Otherwise, include this amount in the total on line 40 on page 2 . . . . .	<b>26</b>			

## Limited Liability Company (LLC)

All states have enacted laws recognizing limited liability companies. An LLC is a separate legal entity you form by filing articles of organization with a state’s Secretary of State. LLCs (and similar entities called Limited Liability Partnerships – LLPs) combine certain features of partnerships with the limited liability feature and other features of corporations.

The individual members are not personally liable for the LLC’s or LLP’s debts or liabilities, except to the extent of their investment and capital commitment in the company. **It is important to note that an LLC/LLP is not a federal tax entity and is generally treated as a partnership by IRS.** A single-member LLC can be treated as a “disregarded entity” for tax purposes, even though still respected as separate for legal purposes. Thus, if owned by an individual, such an entity can be reported as a Schedule C sole proprietorship on the owner’s personal tax return. File Form 8832, ENTITY CLASSIFICATION ELECTION, to state the type of limited liability business organized. For more information on the legal aspects of LLCs/LLPs, contact your Secretary of State’s office. For tax information, see IRS Publication 541, PARTNERSHIPS or the Instructions for Form 1065, PARTNERSHIP RETURN.

## S Corporation

An S Corporation is a small business corporation whose shareholders elect to have corporate income taxed in a manner similar to that of a partnership. Organizing shareholders of a corporation who wish to avoid double taxation may elect to file Form 2553, ELECTION BY A SMALL BUSINESS CORPORATION, to be recognized as an S corporation. This election must be submitted within the first 75 days of the tax year to be permitted for the current tax year. Otherwise, the election is effective for the next tax year. Generally, an S corporation does not pay tax on income resulting from daily operation. Instead, the income and expenses of the corporation are divided among its shareholders (limited to 75), who then report them on their own income tax returns. However, an S corporation does pay taxes on capital gains realized when corporate assets are sold.

An S-corporation has the combined advantages and disadvantages of the partnership and regular corporations.

## S Corporation Files Form 1120S

S corporations file Form 1120S, U.S. INCOME TAX RETURN FOR AN S CORPORATION, and only pay tax on any items that are not passed to shareholders. The S corporation gives each shareholder a Schedule K-1 (Form 1120S), SHAREHOLDER’S SHARE OF INCOME, CREDITS, DEDUCTIONS, ETC. (See Exhibit 1.8 on pages 1-19 and 1-20). The shareholder uses the Schedule K-1 to complete Part II of Schedule

E (Form 1040), and any other forms and schedules the shareholder must file with his or her individual return. Refer to the Instructions for Form 1120S for more information, also see the Instructions for Form 1120S, and Form 2553. Also see Form 1040 Instructions for Schedule E, Part II.

For more information about S corporations, see the Instructions for Form 1120S and Form 2553.

## Corporation

The law treats a corporation as a legal entity. It has a life separate from its owners and has rights and duties of its own. The owners of a corporation are the stockholders. The managers of a corporation may or may not be stockholders. Forming a corporation involves a transfer of money or property, or both, by the prospective shareholders in exchange for capital stock in the corporation. For the purpose of federal income tax, corporations include associations, joint stock companies and trusts and partnerships that actually operate as associations or corporations.

### **Advantages:**

1. The life of the business is perpetual.
2. The stockholders have limited liability.
3. Transfer of ownership is easy (sale of stock).
4. It is easier for corporations to raise capital and to expand than it is for other forms of business.
5. Management may be more efficient.
6. It is adaptable to both small and large businesses.

### **Disadvantages:**

1. It is subject to tax on its income at the corporate level and when the income is distributed as dividends, it is taxed again to the shareholder.
2. It may be more difficult and expensive to organize than other forms of ownership. It is wise to consult an accountant and attorney specializing in corporate law.
3. The corporate charter filed with the Secretary of your state restricts the types of business activities.
4. It is subject to many state and federal controls.

In forming a corporation, a business must organize by applying for a charter through the Secretary of State's office where the principal

business activity will occur. To increase its financial ability, the charter permits corporations to sell stock to numerous shareholders/owners. The corporation is empowered to create debts separate from the shareholders.

Corporation Files  
Either  
Form 1120 or  
1120-A

A corporation takes the same deductions for expenses as a sole proprietor. Special deductions are also available to corporations. Profits of the corporation are taxed to the corporation on either Form 1120-A, U.S. CORPORATION SHORT-FORM INCOME TAX RETURN or Form 1120, U.S. CORPORATION INCOME TAX RETURN, as well as to the shareholders if the profits are distributed. However, shareholders cannot take a loss if the corporation does not operate at a profit. See Exhibit 1.9 for Form 1120-A.

If the corporation paid dividends during the year, it gives each shareholder a Form 1099-DIV, STATEMENT FOR RECIPIENTS OF DIVIDENDS AND DISTRIBUTIONS. A shareholder who works for the corporation is an employee. The corporation gives each employee a Form W-2, WAGE AND TAX STATEMENT. The shareholders and employees use these Forms 1099 DIV and W-2 to complete their individual returns, Form 1040. Publication 542, Corporations, contains additional guidelines.

For more information about corporations, see Publication 542, CORPORATIONS.

EXHIBIT 1.8 - SCHEDULE K-1 (FORM 1120S), PAGE 1

<p><b>SCHEDULE K-1</b> <b>(Form 1120S)</b></p> <p><small>Department of the Treasury Internal Revenue Service</small></p>	<p><b>Shareholder's Share of Income, Credits, Deductions, etc.</b></p> <p>▶ See separate instructions. For calendar year 2001 or tax year , 2001, and ending , 20</p>	<p><small>OMB No. 1545-0130</small></p> <p style="font-size: 24pt; font-weight: bold;">2001</p>	
<p>beginning</p>			
<p><b>Shareholder's identifying number ▶</b> Shareholder's name, address, and ZIP code</p>		<p><b>Corporation's identifying number ▶</b> Corporation's name, address, and ZIP code</p>	
<p><b>A</b> Shareholder's percentage of stock ownership for tax year (see instructions for Schedule K-1) . . . . . ▶ %</p> <p><b>B</b> Internal Revenue Service Center where corporation filed its return ▶ . . . . .</p> <p><b>C</b> Tax shelter registration number (see instructions for Schedule K-1) . . . . . ▶</p> <p><b>D</b> Check applicable boxes: (1) <input type="checkbox"/> Final K-1 (2) <input type="checkbox"/> Amended K-1</p>			
(a) Pro rata share items		(b) Amount	(c) Form 1040 filers enter the amount in column (b) on:
<b>Income (Loss)</b>	1 Ordinary income (loss) from trade or business activities . . . . .	1	} See page 4 of the Shareholder's Instructions for Schedule K-1 (Form 1120S).
	2 Net income (loss) from rental real estate activities . . . . .	2	
	3 Net income (loss) from other rental activities . . . . .	3	
	4 Portfolio income (loss):	4a	} Sch. B, Part I, line 1 Sch. B, Part II, line 5 Sch. E, Part I, line 4 Sch. D, line 5, col. (f) Sch. D, line 12, col. (f) Sch. D, line 12, col. (g) Line 4 of worksheet for Sch. D, line 29 (Enter on applicable line of your return.) See Shareholder's Instructions for Schedule K-1 (Form 1120S). (Enter on applicable line of your return.)
	a Interest . . . . .	4b	
	b Ordinary dividends . . . . .	4c	
	c Royalties . . . . .	4d	
	d Net short-term capital gain (loss) . . . . .	4e(1)	
	e (1) Net long-term capital gain (loss) . . . . .	4e(2)	
	(2) 28% rate gain (loss) . . . . .	4e(3)	
f Other portfolio income (loss) (attach schedule) . . . . .	4f		
5 Net section 1231 gain (loss) (other than due to casualty or theft)	5		
6 Other income (loss) (attach schedule) . . . . .	6		
<b>Deductions</b>	7 Charitable contributions (attach schedule) . . . . .	7	} See page 6 of the Shareholder's Instructions for Schedule K-1 (Form 1120S).
	8 Section 179 expense deduction . . . . .	8	
	9 Deductions related to portfolio income (loss) (attach schedule) . . . . .	9	
	10 Other deductions (attach schedule) . . . . .	10	
<b>Investment Interest</b>	11a Interest expense on investment debts . . . . .	11a	} Form 4952, line 1 See Shareholder's Instructions for Schedule K-1 (Form 1120S).
	b (1) Investment income included on lines 4a, 4b, 4c, and 4f above	11b(1)	
	(2) Investment expenses included on line 9 above . . . . .	11b(2)	
<b>Credits</b>	12a Credit for alcohol used as fuel . . . . .	12a	} Form 6478, line 10 Form 8586, line 5 See pages 6 and 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S).
	b Low-income housing credit:	12b(1)	
	(1) From section 42(j)(5) partnerships . . . . .	12b(2)	
	(2) Other than on line 12b(1) . . . . .	12c	
	c Qualified rehabilitation expenditures related to rental real estate activities . . . . .	12d	
	d Credits (other than credits shown on lines 12b and 12c) related to rental real estate activities . . . . .	12e	
e Credits related to other rental activities . . . . .	12e		
13 Other credits . . . . .	13		

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**EXHIBIT 1.8 - SCHEDULE K-1 (FORM 1120S), PAGE 2**

Schedule K-1 (Form 1120S) 2001		Page <b>2</b>	
(a) Pro rata share items		(b) Amount	
		(c) Form 1040 filers enter the amount in column (b) on:	
<b>Adjustments and Tax Preference Items</b>	<b>14a</b> Depreciation adjustment on property placed in service after 1986	<b>14a</b>	See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S) and Instructions for Form 6251
	<b>b</b> Adjusted gain or loss	<b>14b</b>	
	<b>c</b> Depletion (other than oil and gas)	<b>14c</b>	
	<b>d (1)</b> Gross income from oil, gas, or geothermal properties	<b>14d(1)</b>	
	<b>(2)</b> Deductions allocable to oil, gas, or geothermal properties	<b>14d(2)</b>	
	<b>e</b> Other adjustments and tax preference items (attach schedule)	<b>14e</b>	
<b>Foreign Taxes</b>	<b>15a</b> Name of foreign country or U.S. possession	<b>15a</b>	Form 1116, Part I
	<b>b</b> Gross income from all sources	<b>15b</b>	
	<b>c</b> Gross income sourced at shareholder level	<b>15c</b>	
	<b>d</b> Foreign gross income sourced at corporate level:		
	<b>(1)</b> Passive	<b>15d(1)</b>	
	<b>(2)</b> Listed categories (attach schedule)	<b>15d(2)</b>	
	<b>(3)</b> General limitation	<b>15d(3)</b>	
	<b>e</b> Deductions allocated and apportioned at shareholder level:		
	<b>(1)</b> Interest expense	<b>15e(1)</b>	
	<b>(2)</b> Other	<b>15e(2)</b>	
	<b>f</b> Deductions allocated and apportioned at corporate level to foreign source income:		
<b>(1)</b> Passive	<b>15f(1)</b>		
<b>(2)</b> Listed categories (attach schedule)	<b>15f(2)</b>		
<b>(3)</b> General limitation	<b>15f(3)</b>		
<b>g</b> Total foreign taxes (check one): <input type="checkbox"/> Paid <input type="checkbox"/> Accrued	<b>15g</b>	Form 1116, Part II	
<b>h</b> Reduction in taxes available for credit (attach schedule)	<b>15h</b>	See Instructions for Form 1116	
<b>Other</b>	<b>16</b> Section 59(e)(2) expenditures: <b>a</b> Type	<b>16a</b>	See Shareholder's Instructions for Schedule K-1 (Form 1120S).
	<b>b</b> Amount	<b>16b</b>	Form 1040, line 8b
	<b>17</b> Tax-exempt interest income	<b>17</b>	See page 7 of the Shareholder's Instructions for Schedule K-1 (Form 1120S).
	<b>18</b> Other tax-exempt income	<b>18</b>	
	<b>19</b> Nondeductible expenses	<b>19</b>	
	<b>20</b> Property distributions (including cash) other than dividend distributions reported to you on Form 1099-DIV	<b>20</b>	Form 8611, line 8
	<b>21</b> Amount of loan repayments for "Loans From Shareholders"	<b>21</b>	
<b>22</b> Recapture of low-income housing credit:			
<b>a</b> From section 42(j)(5) partnerships	<b>22a</b>		
<b>b</b> Other than on line 22a	<b>22b</b>		
<b>Supplemental Information</b>	<b>23</b> Supplemental information required to be reported separately to each shareholder (attach additional schedules if more space is needed):		
	.....		
	.....		
	.....		
	.....		
	.....		
	.....		
	.....		
	.....		
	.....		

Exhibit 1.9 Form 1120-A

<b>1120-A</b>		<b>U.S. Corporation Short-Form Income Tax Return</b>		OMB No. 1545-0080	
Form Department of the Treasury Internal Revenue Service		For calendar year 2001 or tax year beginning _____, 2001, ending _____, 20_____		2001	
See separate instructions to make sure the corporation qualifies to file Form 1120-A.					
<b>A</b> Check this box if the corp. is a personal service corp. (as defined in Temporary Regs. section 1.441-4T—see instructions) <input type="checkbox"/>	Use IRS label. Other-wise, print or type.	Name _____ Number, street, and room or suite no. (If a P.O. box, see page 7 of instructions.) _____ City or town, state, and ZIP code _____	<b>B</b> Employer identification number _____ <b>C</b> Date incorporated _____ <b>D</b> Total assets (see page 8 of instructions) \$ _____		
<b>E</b> Check applicable boxes: (1) <input type="checkbox"/> Initial return (2) <input type="checkbox"/> Name change (3) <input type="checkbox"/> Address change <b>F</b> Check method of accounting: (1) <input type="checkbox"/> Cash (2) <input type="checkbox"/> Accrual (3) <input type="checkbox"/> Other (specify) ▶ _____					
	<b>1a</b>	Gross receipts or sales		<b>1c</b>	
		b Less returns and allowances			
		c Balance ▶			
<b>Income</b>	<b>2</b>	Cost of goods sold (see page 14 of instructions).		<b>2</b>	
	<b>3</b>	Gross profit. Subtract line 2 from line 1c		<b>3</b>	
	<b>4</b>	Domestic corporation dividends subject to the 70% deduction		<b>4</b>	
	<b>5</b>	Interest		<b>5</b>	
	<b>6</b>	Gross rents		<b>6</b>	
	<b>7</b>	Gross royalties		<b>7</b>	
	<b>8</b>	Capital gain net income (attach Schedule D (Form 1120))		<b>8</b>	
	<b>9</b>	Net gain or (loss) from Form 4797, Part II, line 18 (attach Form 4797)		<b>9</b>	
	<b>10</b>	Other income (see page 8 of instructions)		<b>10</b>	
	<b>11</b>	Total income. Add lines 3 through 10		<b>11</b>	
	<b>Deductions</b> <small>(See instructions for limitations on deductions.)</small>	<b>12</b>	Compensation of officers (see page 9 of instructions)		<b>12</b>
<b>13</b>		Salaries and wages (less employment credits)		<b>13</b>	
<b>14</b>		Repairs and maintenance		<b>14</b>	
<b>15</b>		Bad debts		<b>15</b>	
<b>16</b>		Rents		<b>16</b>	
<b>17</b>		Taxes and licenses		<b>17</b>	
<b>18</b>		Interest		<b>18</b>	
<b>19</b>		Charitable contributions (see page 10 of instructions for 10% limitation)		<b>19</b>	
<b>20</b>		Depreciation (attach Form 4562)		<b>20</b>	
<b>21a</b>		Less depreciation claimed elsewhere on return		<b>21a</b>	
<b>21b</b>		Total depreciation		<b>21b</b>	
<b>22</b>		Other deductions (attach schedule)		<b>22</b>	
<b>23</b>		Total deductions. Add lines 12 through 22		<b>23</b>	
<b>24</b>		Taxable income before net operating loss deduction and special deductions. Subtract line 23 from line 11		<b>24</b>	
<b>25a</b>		Less: a Net operating loss deduction (see page 13 of instructions)		<b>25a</b>	
<b>25b</b>	b Special deductions (see page 13 of instructions)		<b>25b</b>		
<b>25c</b>	Total special deductions		<b>25c</b>		
<b>26</b>	Taxable income. Subtract line 25c from line 24		<b>26</b>		
<b>27</b>	Total tax (from page 2, Part I, line 8)		<b>27</b>		
<b>Tax and Payments</b>	<b>28 Payments:</b>				
	<b>28a</b>	a 2000 overpayment credited to 2001		<b>28a</b>	
	<b>28b</b>	b 2001 estimated tax payments		<b>28b</b>	
	<b>28c</b>	c Less 2001 refund applied for on form 4466		<b>28c</b>	
	<b>28d</b>	d Total payments		<b>28d</b>	
	<b>28e</b>	e Tax deposited with Form 7004		<b>28e</b>	
	<b>28f</b>	f Credit for tax paid on undistributed capital gains (attach Form 2439)		<b>28f</b>	
	<b>28g</b>	g Credit for Federal tax on fuels (attach Form 4136). See instructions		<b>28g</b>	
	<b>28h</b>	h Total payments. Add lines 28d through 28g		<b>28h</b>	
	<b>29</b>	Estimated tax penalty (see page 14 of instructions). Check if Form 2220 is attached <input type="checkbox"/>		<b>29</b>	
<b>30</b>	Tax due. If line 28h is smaller than the total of lines 27 and 29, enter amount owed		<b>30</b>		
<b>31</b>	Overpayment. If line 28h is larger than the total of lines 27 and 29, enter amount overpaid		<b>31</b>		
<b>32</b>	Enter amount of line 31 you want: Credited to 2002 estimated tax ▶ _____ Refunded ▶ _____		<b>32</b>		
Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.					
<b>Sign Here</b>	Signature of officer _____	Date _____	Title _____	May the IRS discuss this return with the preparer shown below (see instructions)? <input type="checkbox"/> Yes <input type="checkbox"/> No	
<b>Paid Preparer's Use Only</b>	Preparer's signature ▶ _____	Date _____	Check if self-employed <input type="checkbox"/>	Preparer's SSN or PTIN _____	
	Firm's name for yours if self-employed, address, and ZIP code ▶ _____	EIN _____	Phone no. ( ) _____		
For Paperwork Reduction Act Notice, see page 20 of the instructions. Cat. No. 11456E Form 1120-A (2001)					

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## Net Profit or Loss

To figure estimated taxes and to report income earned from your business, you must figure your profit or loss. Profit is the amount on which you will pay tax. If you operated at a loss, the amount is entered in parenthesis and will reduce other income. The basic way to determine profit or loss is the same for each type of business organization.

$$\text{Gross Income} - \text{Expenses} = \text{Net profit or loss}$$

You will use this formula with some slight changes to determine your profit or loss on your tax return. This workbook expands the formula by discussing gross receipts and cost of goods sold, both of which are used in determining gross income for either type of business. Since many new businesses start as a sole proprietor, the following illustrates the preparation of Schedule C, Profit or Loss From Business (Sole Proprietor).

### Gross Receipts or Sales

Gross receipts or sales are the income that a business receives from sales of its products or services. **Gross receipts less returns and allowances equal net sales.** In the example illustrated in this lesson, John's Furniture Store sales for the year were \$48,000 with neither returns nor allowances. Therefore, the store had \$48,000 in both gross receipts (line 1) and net receipts (line 3).

### Cost of Goods Sold

Cost of goods sold is the cost to a business to buy or make the product that it sold. It is easy to figure the cost of goods sold if you sell all your merchandise during the year. However, some of your sales will probably be from inventory that you carried over from earlier years and you will probably have inventory left unsold at the end of the year.

To figure the cost of goods sold, start with the value of the inventory on hand at the beginning of the year. Add the cost of goods purchased or manufactured during the year. Subtract the cost of any merchandise withdrawn for personal use. The result is the cost of items available for sale during the year. Then subtract the value of your inventory at the end of the year; your cost of goods sold is the remainder. This can be stated by the following formula:

$$\begin{array}{r}
 \text{Beginning inventory} \\
 + \text{Purchases} \\
 \hline
 = \text{Cost of items Available} \\
 - \text{Ending inventory} \\
 \hline
 = \text{Cost of goods sold}
 \end{array}$$

For example, John's Furniture Store shows the following in Part III of Schedule C: an inventory of \$12,000 at the beginning of the



year (line 35), purchased furniture costing \$26,000 during the year (line 36) and an ending inventory of \$9,800 (line 41). The cost of goods sold was \$28,200 (line 42) that is also written on line 4 in Part 1 of Schedule C. Using the formula, this is stated as:

<b>Beginning inventory</b>	<b>\$12,000</b>
<b>+ Purchases</b>	<b>+ 26,000</b>
<b>= <u>Cost of items Available</u></b>	<b>= <u>38,000</u></b>
<b>- <u>Ending inventory</u></b>	<b>- <u>9,800</u></b>
<b>= <u>Cost of goods sold</u></b>	<b>= <u>28,200</u></b>

### Gross Profit

Gross profit equals the net receipts (the balance of gross receipts less returns and allowances) less the cost of goods sold. John's Furniture Store had gross (and net) receipts of \$48,000 (lines 1 and 3) and the cost of goods sold was \$28,200 (line 4). The store's gross profit was \$19,800 ( $\$48,000 - \$28,200 = \$19,800$ ) on line 7 of Schedule C. After you determine the income, you must determine the expenses, which is the other item in the formula for computing profit or loss.

### Business Expenses

Business expenses are the ordinary and necessary expenses for the operation of a business. The cost of business property that has a life of more than 1 year, such as a truck or a building, is not considered a current business expense. That cost is usually deducted on your tax return over a number of years as depreciation (discussed later). John's Furniture Store had total expense of \$11,000 of which \$10,800 was current business expenses and \$200 was depreciation. This would be reported on his line 28 of the Schedule C.

### Net Profit or Loss

Net profit or loss is the amount by which the gross profit and any other income for a period is more (or less, in the case of a loss) than the business expenses and depreciation for the same period. John's Furniture Store had a gross profit of \$19,800 (line 7) and business expenses of \$11,000 (line 28). The store's net profit was \$8,800 ( $\$19,800 - \$11,000 = \$8,800$ ) on line 31 of Schedule C. A sole proprietor or member of a partnership must pay self-employment taxes on the net profit; in this example, on the \$8,800. The computation of the self-employment tax is on Schedule SE. A filled-in Schedule C and SE, the forms for a sole proprietorship, are shown as examples. (See Exhibits 1.10, 1.11 and 1.12.)

**Note:** *You may be able to file the shorter Schedule C-EZ, if you meet certain requirements. For more information, see Schedule C-EZ and Exhibit 1.13 on page 1-27.*

**EXHIBIT 1.10 - SCHEDULE C, P G. 1, JOHN MARTIN EXAMPLE**

<p><b>SCHEDULE C</b> <b>(Form 1040)</b></p> <p>Department of the Treasury Internal Revenue Service (99)</p>	<p><b>Profit or Loss From Business</b> (Sole Proprietorship)</p> <p>▶ Partnerships, joint ventures, etc., must file Form 1065 or 1065-B. ▶ Attach to Form 1040 or 1041. ▶ See Instructions for Schedule C (Form 1040).</p>	<p>OMB No. 1545-0074</p> <p><b>2002</b> Attachment Sequence No. <b>09</b></p>	
<p>Name of proprietor <b>John M. Martin</b></p>		<p>Social security number (SSN) <b>123 00 1234</b></p>	
<p><b>A</b> Principal business or profession, including product or service (see page C-1 of the instructions) <b>Retail Furniture</b></p>		<p><b>B</b> Enter code from pages C-7, 8, &amp; 9 <b>4 4 2 1 1 0</b></p>	
<p><b>C</b> Business name. If no separate business name, leave blank. <b>John's Furniture Mart</b></p>		<p><b>D</b> Employer ID number (EIN), if any <b>1 0 0 1 0 1 0 1 0</b></p>	
<p><b>E</b> Business address (including suite or room no.) ▶ <b>23 Valley Street</b> City, town or post office, state, and ZIP code <b>Lake City, MD 21235</b></p>			
<p><b>F</b> Accounting method: (1) <input checked="" type="checkbox"/> Cash (2) <input type="checkbox"/> Accrual (3) <input type="checkbox"/> Other (specify) ▶</p>			
<p><b>G</b> Did you "materially participate" in the operation of this business during 2002? If "No," see page C-3 for limit on losses <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No</p>			
<p><b>H</b> If you started or acquired this business during 2002, check here <input type="checkbox"/></p>			
<b>Part I Income</b>			
<p><b>1</b> Gross receipts or sales. <b>Caution.</b> If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see page C-3 and check here <input type="checkbox"/></p>	<b>1</b>	<b>48,000</b>	<b>00</b>
<b>2</b> Returns and allowances	<b>2</b>		
<b>3</b> Subtract line 2 from line 1	<b>3</b>	<b>48,000</b>	<b>00</b>
<b>4</b> Cost of goods sold (from line 42 on page 2)	<b>4</b>	<b>28,200</b>	<b>00</b>
<b>5</b> <b>Gross profit.</b> Subtract line 4 from line 3	<b>5</b>	<b>19,800</b>	<b>00</b>
<b>6</b> Other income, including Federal and state gasoline or fuel tax credit or refund (see page C-3)	<b>6</b>		
<b>7</b> <b>Gross income.</b> Add lines 5 and 6	<b>7</b>	<b>19,800</b>	<b>00</b>
<b>Part II Expenses.</b> Enter expenses for business use of your home <b>only</b> on line 30.			
<b>8</b> Advertising	<b>8</b>		
<b>9</b> Bad debts from sales or services (see page C-3)	<b>9</b>		
<b>10</b> Car and truck expenses (see page C-3)	<b>10</b>		
<b>11</b> Commissions and fees	<b>11</b>		
<b>12</b> Depletion	<b>12</b>		
<b>13</b> Depreciation and section 179 expense deduction (not included in Part III) (see page C-4)	<b>13</b>		
<b>14</b> Employee benefit programs (other than on line 19)	<b>14</b>		
<b>15</b> Insurance (other than health)	<b>15</b>		
<b>16</b> Interest:	<b>16</b>		
<b>a</b> Mortgage (paid to banks, etc.)	<b>16a</b>		
<b>b</b> Other	<b>16b</b>		
<b>17</b> Legal and professional services	<b>17</b>		
<b>18</b> Office expense	<b>18</b>		
<b>19</b> Pension and profit-sharing plans	<b>19</b>		
<b>20</b> Rent or lease (see page C-5):	<b>20</b>		
<b>a</b> Vehicles, machinery, and equipment	<b>20a</b>		
<b>b</b> Other business property	<b>20b</b>		
<b>21</b> Repairs and maintenance	<b>21</b>	<b>300</b>	<b>00</b>
<b>22</b> Supplies (not included in Part III)	<b>22</b>	<b>1,300</b>	<b>00</b>
<b>23</b> Taxes and licenses	<b>23</b>		
<b>24</b> Travel, meals, and entertainment:	<b>24</b>		
<b>a</b> Travel	<b>24a</b>		
<b>b</b> Meals and entertainment	<b>24b</b>		
<b>c</b> Enter nondeductible amount included on line 24b (see page C-5)	<b>24c</b>		
<b>d</b> Subtract line 24c from line 24b	<b>24d</b>		
<b>25</b> Utilities	<b>25</b>		
<b>26</b> Wages (less employment credits)	<b>26</b>	<b>5,000</b>	<b>00</b>
<b>27</b> Other expenses (from line 48 on page 2)	<b>27</b>	<b>50</b>	<b>00</b>
<b>28</b> <b>Total expenses</b> before expenses for business use of home. Add lines 8 through 27 in columns	<b>28</b>	<b>11,000</b>	<b>00</b>
<b>29</b> Tentative profit (loss). Subtract line 28 from line 7	<b>29</b>	<b>8,800</b>	<b>00</b>
<b>30</b> Expenses for business use of your home. Attach <b>Form 8829</b>	<b>30</b>		
<b>31</b> <b>Net profit or (loss).</b> Subtract line 30 from line 29.	<b>31</b>	<b>8,800</b>	<b>00</b>
<p>• If a profit, enter on <b>Form 1040, line 12</b>, and also on <b>Schedule SE, line 2</b> (statutory employees, see page C-6). Estates and trusts, enter on Form 1041, line 3.</p> <p>• If a loss, you <b>must</b> go to line 32.</p>			
<p><b>32</b> If you have a loss, check the box that describes your investment in this activity (see page C-6).</p> <p>• If you checked 32a, enter the loss on <b>Form 1040, line 12</b>, and also on <b>Schedule SE, line 2</b> (statutory employees, see page C-6). Estates and trusts, enter on Form 1041, line 3.</p> <p>• If you checked 32b, you <b>must</b> attach <b>Form 6198</b>.</p>			
		<p><b>32a</b> <input type="checkbox"/> All investment is at risk.</p> <p><b>32b</b> <input type="checkbox"/> Some investment is not at risk.</p>	

**EXHIBIT 1.11 - SCHEDULE C, P G. 2, JOHN MARTIN EXAMPLE**

Schedule C (Form 1040) 2002

Page **2**

**Part III Cost of Goods Sold** (see page C-6)

33 Method(s) used to value closing inventory:    **a**  Cost                      **b**  Lower of cost or market                      **c**  Other (attach explanation)

34 Was there any change in determining quantities, costs, or valuations between opening and closing inventory? If "Yes," attach explanation . . . . .  **Yes**                       **No**

35	Inventory at beginning of year. If different from last year's closing inventory, attach explanation . . . . .	35	12,000	00
36	Purchases less cost of items withdrawn for personal use . . . . .	36	26,000	00
37	Cost of labor. Do not include any amounts paid to yourself . . . . .	37		
38	Materials and supplies . . . . .	38		
39	Other costs . . . . .	39		
40	Add lines 35 through 39 . . . . .	40	38,000	00
41	Inventory at end of year . . . . .	41	9,800	00
42	<b>Cost of goods sold.</b> Subtract line 41 from line 40. Enter the result here and on page 1, line 4 . . . . .	42	28,200	00

**Part IV Information on Your Vehicle.** Complete this part **only** if you are claiming car or truck expenses on line 10 and are not required to file Form 4562 for this business. See the instructions for line 13 on page C-4 to find out if you must file.

43 When did you place your vehicle in service for business purposes? (month, day, year) ▶ 06 / 07 / 1996

44 Of the total number of miles you drove your vehicle during 2002, enter the number of miles you used your vehicle for:

**a** Business 4,500                      **b** Commuting 1,500                      **c** Other 7,000

45 Do you (or your spouse) have another vehicle available for personal use? . . . . .  **Yes**                       **No**

46 Was your vehicle available for personal use during off-duty hours? . . . . .  **Yes**                       **No**

47a Do you have evidence to support your deduction? . . . . .  **Yes**                       **No**

**b** If "Yes," is the evidence written? . . . . .  **Yes**                       **No**

**Part V Other Expenses.** List below business expenses not included on lines 8–26 or line 30.

		50	00
48	<b>Total other expenses.</b> Enter here and on page 1, line 27 . . . . .	48	50 00



Schedule C (Form 1040) 2002

**EXHIBIT 1.12 - SCHEDULE SE, JOHN MARTIN EXAMPLE**

<p><b>SCHEDULE SE</b> <b>(Form 1040)</b></p> <p><small>Department of the Treasury Internal Revenue Service (99)</small></p>	<p><b>Self-Employment Tax</b></p> <p>▶ Attach to Form 1040. ▶ See Instructions for Schedule SE (Form 1040).</p>	<p><small>OMB No. 1545-0074</small></p> <p style="font-size: 24pt; font-weight: bold;">2002</p> <p><small>Attachment Sequence No. 17</small></p>
<p>Name of person with <b>self-employment</b> income (as shown on Form 1040) <b>John M. Martin</b></p>		<p>Social security number of person with <b>self-employment</b> income ▶ <b>123 00 1234</b></p>

**Who Must File Schedule SE**

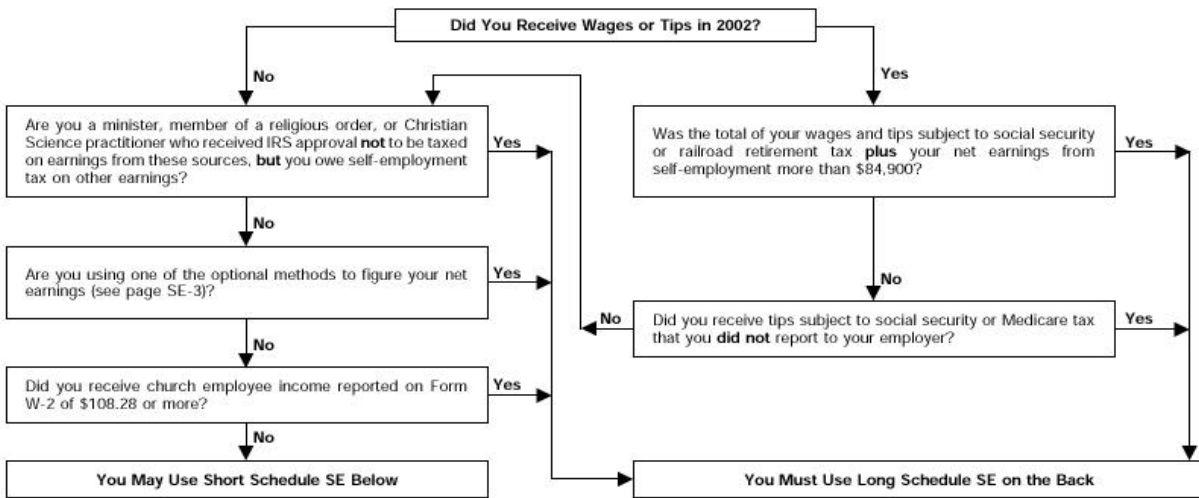
You must file Schedule SE if:

- You had net earnings from self-employment from **other than** church employee income (line 4 of Short Schedule SE or line 4c of Long Schedule SE) of \$400 or more **or**
- You had church employee income of \$108.28 or more. Income from services you performed as a minister or a member of a religious order **is not** church employee income. See page SE-1.

**Note.** Even if you had a loss or a small amount of income from self-employment, it may be to your benefit to file Schedule SE and use either "optional method" in Part II of Long Schedule SE. See page SE-3.

**Exception.** If your only self-employment income was from earnings as a minister, member of a religious order, or Christian Science practitioner **and** you filed Form 4361 and received IRS approval not to be taxed on those earnings, **do not** file Schedule SE. Instead, write "Exempt-Form 4361" on Form 1040, line 56.

**May I Use Short Schedule SE or Must I Use Long Schedule SE?**



**Section A—Short Schedule SE. Caution.** Read above to see if you can use Short Schedule SE.

<b>1</b> Net farm profit or (loss) from Schedule F, line 36, and farm partnerships, Schedule K-1 (Form 1065), line 15a	<b>1</b>			
<b>2</b> Net profit or (loss) from Schedule C, line 31; Schedule C-EZ, line 3; Schedule K-1 (Form 1065), line 15a (other than farming); and Schedule K-1 (Form 1065-B), box 9. Ministers and members of religious orders, see page SE-1 for amounts to report on this line. See page SE-2 for other income to report	<b>2</b>	8,800	00	
<b>3</b> Combine lines 1 and 2	<b>3</b>	8,800	00	
<b>4</b> <b>Net earnings from self-employment.</b> Multiply line 3 by 92.35% (.9235). If less than \$400, do not file this schedule; you do not owe self-employment tax ▶	<b>4</b>	8,127	00	
<b>5</b> <b>Self-employment tax.</b> If the amount on line 4 is: <ul style="list-style-type: none"> <li>• \$84,900 or less, multiply line 4 by 15.3% (.153). Enter the result here and on <b>Form 1040, line 56.</b></li> <li>• More than \$84,900, multiply line 4 by 2.9% (.029). Then, add \$10,527.60 to the result. Enter the total here and on <b>Form 1040, line 56.</b></li> </ul>	<b>5</b>	1,243	00	
<b>6</b> <b>Deduction for one-half of self-employment tax.</b> Multiply line 5 by 50% (.5). Enter the result here and on <b>Form 1040, line 29</b>	<b>6</b>	622	00	



**EXHIBIT 1.13 -BLANK SCHEDULE C-EZ**

<p><b>SCHEDULE C-EZ (Form 1040)</b></p> <p><small>Department of the Treasury Internal Revenue Service (99)</small></p>	<p><b>Net Profit From Business</b> (Sole Proprietorship)</p> <p>▶ Partnerships, joint ventures, etc., must file Form 1065 or 1065-B. ▶ Attach to Form 1040 or 1041. ▶ See instructions on back.</p>	<p><small>OMB No. 1545-0074</small></p> <p style="font-size: 2em; font-weight: bold;">2002</p> <p><small>Attachment Sequence No. 09A</small></p>
<p>Name of proprietor</p>		<p>Social security number (SSN)</p>

**Part I General Information**

**You May Use Schedule C-EZ Instead of Schedule C Only If You:**

- Had business expenses of \$2,500 or less.
- Use the cash method of accounting.
- Did not have an inventory at any time during the year.
- Did not have a net loss from your business.
- Had only one business as a sole proprietor.

And You:

- Had no employees during the year.
- Are not required to file **Form 4562**, Depreciation and Amortization, for this business. See the instructions for Schedule C, line 13, on page C-4 to find out if you must file.
- Do not deduct expenses for business use of your home.
- Do not have prior year unallowed passive activity losses from this business.

<p><b>A</b> Principal business or profession, including product or service</p>	<p><b>B</b> Enter code from pages C-7, 8, &amp; 9</p>
<p><b>C</b> Business name. If no separate business name, leave blank.</p>	<p><b>D</b> Employer ID number (EIN), if any</p>
<p><b>E</b> Business address (including suite or room no.). Address not required if same as on Form 1040, page 1.</p> <p>City, town or post office, state, and ZIP code</p>	

**Part II Figure Your Net Profit**

<p><b>1 Gross receipts. Caution.</b> If this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked, see <b>Statutory Employees</b> in the instructions for Schedule C, line 1, on page C-3 and check here <input type="checkbox"/></p>	1	
<p><b>2 Total expenses</b> (see instructions). If more than \$2,500, you <b>must</b> use Schedule C</p>	2	
<p><b>3 Net profit.</b> Subtract line 2 from line 1. If less than zero, you <b>must</b> use Schedule C. Enter on <b>Form 1040, line 12</b>, and also on <b>Schedule SE, line 2</b>. (Statutory employees <b>do not</b> report this amount on Schedule SE, line 2. Estates and trusts, enter on Form 1041, line 3.)</p>	3	

**Part III Information on Your Vehicle.** Complete this part **only** if you are claiming car or truck expenses on line 2.

- 4 When did you place your vehicle in service for business purposes? (month, day, year) ▶ ...../...../.....
- 5 Of the total number of miles you drove your vehicle during 2002, enter the number of miles you used your vehicle for:
  - a Business .....
  - b Commuting .....
  - c Other .....
- 6 Do you (or your spouse) have another vehicle available for personal use?  Yes  No
- 7 Was your vehicle available for personal use during off-duty hours?  Yes  No
- 8a Do you have evidence to support your deduction?  Yes  No
  - b If "Yes," is the evidence written?  Yes  No

## Business Tax Returns

### Self-Employment Tax

Self-employed people who are sole proprietors or partners in a partnership are subject to self-employment (SE) tax if they have \$400 or more in net earnings from self-employment income. In 2002, the tax rate for self-employment tax is 15.3% of which 12.4% is social security (old age, survivors and disability insurance) plus 2.9% for Medicare (hospital insurance). As an employee, you pay one half of these taxes and your employer pays the other one half. If you are also an employee, you may still be required to pay these taxes on self-employed income.



**Income passed through to shareholders of an S Corporation is not subject to self-employment tax.**

*Note: The maximum net earnings subject to the social security tax for 2002 is \$84,900. There is no maximum limit on the amount subject to the 2.9% Medicare tax.*

If you receive wages in 2002 from which Social Security and Medicare taxes are withheld, subtract those wages from the maximums to figure how much self-employment income is subject to the taxes. For example, in 2002 you receive wages of \$50,000 from your employer and net \$35,000 in self-employment income. You would first subtract your wages, \$50,000, from the social security maximum, of \$84,900. Only \$34,900 of your self-employment income is subject to the 12.4% Social Security portion of the self-employment tax. All of the \$35,000 is subject to the 2.9% Medicare Tax.

If you have income subject to self-employment tax, figure the tax on Schedule SE (Form 1040), SELF-EMPLOYMENT TAX. If you have more than one business, use one Schedule SE and combine the profits and losses from all of your businesses. You must file Schedule SE if:

- your net earnings from self-employment are \$400 or more, or
- you had church employee income of \$108.28 or more.

*Note: If you are a member of the clergy or a religious worker, you may not have to pay self-employment tax if you meet certain exemption requirements.*

Schedule SE is shown later in this lesson. For more information, see Form 1040 Instructions and Publication 533, SELF-EMPLOYMENT TAX.

## Estimated Tax

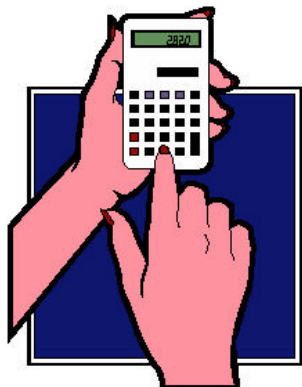
Many sole proprietors, partners and S corporation shareholders must pay estimated taxes during the year. To determine if you must pay it, estimate your taxable income for the year. Include your self-employment income and all other taxable income. Also estimate how much of your income will be subject to withholding.

Your estimated tax is the amount by which the total of your estimated income tax and self-employment tax exceeds the tax you expect to have withheld from your wages, if any. You do not have to pay estimated tax if you reasonably expect your estimated tax owed to be less than \$1,000.

Use the worksheet that comes with Form 1040-ES, ESTIMATED TAX FOR INDIVIDUALS, or the Annualized Worksheet in Publication 505, TAX WITHHOLDING AND ESTIMATED TAX, to figure the amount and decide if you must pay estimated tax. Corporations figure their estimated tax on Form 1120-W (Worksheet), ESTIMATED TAX FOR CORPORATIONS.



## Business Deductions and Credits



In place of deductions for expenses to reduce the profit of the business, a business may elect to claim all or part of the eligible business expense as a tax credit. Although both deductions and credits lower your tax, they differ. **Deductions** are subtracted from income, and **credits** are subtracted from tax. Often it is best to compute the item each way—as a deduction, then a new computation omitting the item as an expense, but figuring it as a credit. Select the method that accurately gives the greater benefit. Caution: the same expense and dollar amount cannot be used for both a deduction and credit.

The **Work Opportunity Credit (Form 5884)** and the **Welfare-to-Work Credit (Form 8861)** are of particular interest to those who already have, or are thinking about having, employees. The Work Opportunity Credit provides an incentive to hire individuals from targeted groups that have a particularly high unemployment rate or other special employment needs. The amount of the credit depends on when the individual began working for you, generally before January 1, 2004. For more information, see Form 8861, **WELFARE-TO-WORK CREDIT**.

The Welfare-to-Work Credit is a credit that you can take for qualified wages you pay to qualified long-term family assistance recipients who started working for you after December 31, 1997 and before January 1, 2004.

You must receive certification from your state employment security agency before claiming either credit. Submit **Form 8850, PRESCREENING NOTICE AND CERTIFICATION REQUEST FOR THE WORK OPPORTUNITY AND WELFARE-TO-WORK CREDITS**, no later than 21 days after the employee begins working for you. For more information, see Publication 954, **TAX INCENTIVES FOR EMPOWERMENT ZONES AND OTHER DISTRESSED COMMUNITIES** contains the requirements for these and other credits.

Travel,  
Transportation  
and  
Entertainment  
Expenses

**Travel expenses** are the ordinary and necessary expenses for traveling overnight away from home in the course of your trade or business. These expenses include the cost of public transportation, operating and maintaining your car, meals, lodging and other related expenses.



**Transportation expenses** are the ordinary and necessary expenses of getting from one workplace to another in the course of your business or profession, while you are not away from home. Business entertainment expenses are deductible only if they are ordinary and necessary expenses of carrying on your trade or business and you can prove them.

For more information, see Publication 334 and Publication 463, TRAVEL, ENTERTAINMENT, GIFT AND CAR EXPENSES.

## Car Expenses

If you use a car for business only, you may base your deduction on the full cost of operating it. If you use the car for both business and personal purposes, you must divide your expenses between those uses on the basis of mileage to compute a business percentage. Do not include commuting to and from work as business mileage.

You may take a deduction for your actual business expenses for the car, or use a standard mileage rate. However, to use the standard mileage rate on a vehicle after the first year of business use, you must have used the standard mileage rate the first year. In later years you can alternate between standard mileage and actual expenses. This alternating option is not available to you if actual expenses are claimed the first year of business use. Under either system, parking fees, and tolls are deductible. Actual business expenses include gas, oil, repairs, insurance, depreciation, tires and license plates. In 2001, the standard mileage rate was 34.5¢ per business mile, the rate increased to 36.5 cents for the year 2002.

For more information, refer to Publication 463 also read Publication 946, HOW TO DEPRECIATE PROPERTY.

## Business Use of Your Home

If you use part of your home in your business regularly and exclusively, you may be able to claim part of the expenses of maintaining your home as a business expense. Special rules apply if you use part of your home as a day care center or to store inventory. These expenses include mortgage interest, insurance, utilities, repairs and depreciation or rent. The business use of your home must meet certain other requirements before you can take any of these expenses as business deductions.

To deduct your expenses for business use of your home if you are self-employed, use Schedule C (Form 1040) and Form 8829, EXPENSES FOR BUSINESS USE OF YOUR HOME. An employee must use line 20 of Schedule A (Form 1040), to itemize this miscellaneous deduction. For more information, see Publication 587, BUSINESS USE OF YOUR HOME, and Lesson 4 in this workbook.

## Retirement Plans

If you establish a retirement arrangement for yourself and/or your employees, you may be able to take a deduction for your contributions to the plan. The plans discussed here are popular among up-and-coming businesses.

As a plan for yourself, you can establish a traditional individual retirement arrangement (IRA) or the new Roth IRA. If you are a sole proprietor or a member of a partnership, you can have a qualified plan. If requirements are met, you may not be taxed on certain amounts you pay into the plan, or on the plan's earnings, until they are distributed to you in future years. Many employers elect to include employees in their qualified plan.

If you have employees, both you and they can set up simplified employee pensions (SEPs). A SEP is a kind of IRA that was designed for employers whose employees have worked for them at least 3 years; the SEP has very few administrative burdens or costs.

You can set up and contribute up to 15% of his or her earnings to a SEP for each of your employees, then deduct the contribution (up to \$40,000 for the 2002 tax year).

Another option is you can set up a savings incentive-matching plan for employees called a SIMPLE plan if you have 100 or fewer employees and meet several other requirements. Under this plan, the employer makes contributions to employees' IRAs. The two types of plans are the SIMPLE IRA and SIMPLE 401(k).

For more information on these pension plan options, see Publication 590, *INDIVIDUAL RETIREMENT ARRANGEMENTS (IRAs) AND QUALIFIED PLANS* and Publication 560, *RETIREMENT PLANS FOR SMALL BUSINESS (SEP, SIMPLE AND QUALIFIED PLANS)*.

## Health Insurance Deduction for the Self-Employed

If not otherwise covered by an employer's subsidized health insurance plan, you may be able to deduct 70% (100% in the years 2003 and later) of the amount you paid for medical insurance for yourself and your family. You deduct this amount in the "Adjustment" section on the front of on line 28 of Form 1040 (2001). For more information including a worksheet, see Chapter 7 in Publication 535, *BUSINESS EXPENSES*.

## Business Start-Up Costs

Start-up costs are those expenses that you have in connection with setting up an active trade or business, or for investigating the possibility of creating or acquiring an active trade or business.

## Depreciation and Section 179

Generally, you can amortize these costs over a 60-month period after you begin operating your business. For more information, see Chapter 9 of Publication 535.

If you buy property for use in your business that has a life of more than 1 year, you may deduct its cost or other basis over a number of years. This practice is called depreciation. Do not depreciate land, inventory, or property you placed in service and disposed of in the same year.

### Depreciation of Business Property



You can depreciate property that meets all of the following basic requirements:

- the property must be used in business or held for the production of income,
- the property must have a determinable useful life which must be longer than one year, and
- the property must be something that wears out, decays, gets used up, becomes obsolete or loses value from natural causes.

The method for depreciating most tangible property placed in service after 1986 is the Modified Accelerated Cost Recovery System (MACRS). Note: Tangible property is any property that can be seen or touched, like buildings, cars, machinery or equipment.

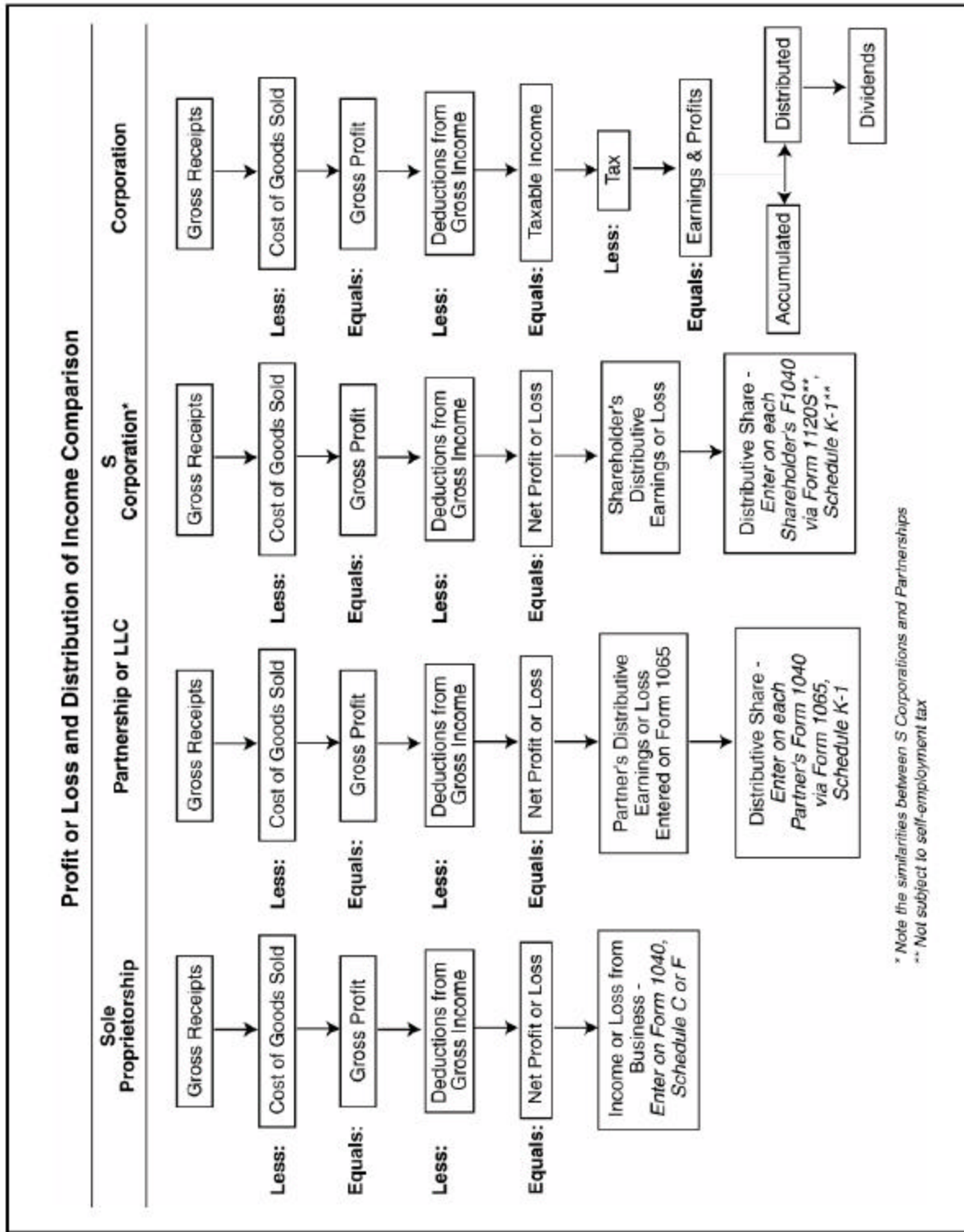
### Section 179 Deduction

You can choose to deduct a limited amount (for 2000, up to \$20,000; for 2001 and up to \$24,000 for 2002 tax year) of the cost of certain depreciable property in the year you buy it for use in your business. This deduction is known as the “section 179 deduction.”

Use Form 4562, *DEPRECIATION AND AMORTIZATION*, to figure your section 179 deduction. Publication 946 explains what costs you can and cannot deduct, how to figure the MACRS deduction for depreciation and Section 179 and when to recapture the deductions.

Pub.535 discusses specific business expense deductions and Pub. 954, *TAX INCENTIVES*, discusses credits you may be eligible to claim towards reducing federal taxes on profits of your business.

EXHIBIT 1.11 - PROFIT OR LOSS AND DISTRIBUTION OF INCOME COMPARISON



**EXHIBIT 1.12 - BUSINESS REQUIREMENTS AT A GLANCE**

<b>If you're a:</b>	<b>You may be liable for:</b>	<b>Use form:</b>
Sole Proprietor or single member LLC	Income Tax	1040, Sch. C <sup>1</sup> or C-EZ
	Self-employment tax	1040, Sch. SE
	Estimated tax	1040-ES
	Employment taxes:  • Social security, Medicare, income tax withholding  • Federal Unemployment (FUTA) Tax  • Depositing employment taxes	941  940 or 940-EZ  8109 <sup>2</sup>
Partnership or LLC	Annual return of income	1065, Sch. K-1
	Employment taxes	Same as sole proprietor
Partner in a partnership (individual)	Income tax	1040 and Sch. E <sup>3</sup>
	Self-employment tax	1040 and Sch. SE
	Estimated tax	1040-ES
Corporation or S Corporation	Income tax	1120 or 1120-A (corp.) 1120S (S Corporation)
	Estimated tax	1120-W (corp. only and 8109)
	Employment taxes	Same as sole proprietor
S Corporation shareholder	Income tax	1040 and Sch. E <sup>3</sup>
	Estimated tax	1040-ES
<sup>1</sup> File a separate schedule for each business. <sup>2</sup> Do not use if you deposit taxes electronically. <sup>3</sup> Various other schedules may be needed.		

All IRS forms and publications can be downloaded from the INTERNET at [www.irs.gov/prod/forms\\_pubs/index.html](http://www.irs.gov/prod/forms_pubs/index.html) ordered free by calling 1-800-829-3676. Or, you can buy a CDROM of current and prior year tax forms and publications from the National Technical Information Service (toll free at 1-877-233-6767 or on-line at [www.irs.gov/cdorders](http://www.irs.gov/cdorders). You can also get forms via fax. (From your fax machine dial 703-368-9694.)

**MOST COMMONLY USED FEDERAL TAX FORMS REQUIRED TO BE SENT TO IRS** Reading the publications that precede the forms and instructions to the forms provide help to prepare these forms. View all of the publications with your own copy of Publication 1796 Tax Products. This CDROM contains all of the forms and publications mentioned in this workbook. Publication 1796 can be ordered, a fee may be charged. **To read a summary of each publications content and to learn more about IRS, read Publication 910, IRS GUIDE TO FREE TAX SERVICES.**

Publication 1, YOUR RIGHTS AS A TAXPAYER

Publication 15, Circular E, EMPLOYER'S TAX GUIDE

Publication 15-A, EMPLOYER'S SUPPLEMENTAL TAX GUIDE

Publication 15-B, EMPLOYER'S TAX GUIDE TO FRINGE BENEFITS

**Form 940, Federal Unemployment Tax,**

**Form 941, Employers Quarterly Tax Return**

Publication 51, Circular A, AGRICULTURAL EMPLOYER'S TAX GUIDE

**Form 943, Employer's Annual Tax Return for Agriculture Employees**

Publication 225, FARMER'S TAX GUIDE

**Forms 1040 (Schedules A, D, F, J, SE), 4136, 4562, 4684, 4797, 6251**

Publication 334, TAX GUIDE FOR SMALL BUSINESS (FOR INDIVIDUALS WHO USE SCHEDULE C OR C-EZ)

Publication 535, BUSINESS EXPENSES

**Form 1040 (Schedules C, C-EZ (Profit and Loss for Sole Proprietors**

Publication 378, FUEL TAX CREDITS AND REFUNDS,

**Forms 720 Quarterly Federal Excise, 4136 Credit Tax on Fuel, 8849 Sales by Gasoline Wholesale Distributors**

Publication 463, TRAVEL, ENTERTAINMENT, GIFT AND CAR EXPENSES

**Forms 2106, 2106EZ Employee Business Expenses**

Publication 505, TAX WITHHOLDING AND ESTIMATED TAX

**Estimated Tax Payments Forms 1040-ES, 2210, 2210F, Federal Tax Withholding W-4, W-4P**

Publication 509, TAX CALENDARS FOR 2002  
Publication 510, EXCISE TAXES FOR 2002  
**Forms 11-C (Registration for Wagering), 637, 720 Quarterly Federal Excise Tax, 730 Tax on Wagering, 6197 Gas Guzzler, 6627 Environmental Tax**  
Publication 533, SELF-EMPLOYMENT TAX  
**Form 1040 (Schedule SE) Self-Employment Tax** Publication 534, DEPRECIATING PROPERTY PLACED IN SERVICE BEFORE 1987  
Publication 946 HOW TO DEPRECIATE PROPERTY (Section 179, MACRS, Listed Property)  
**Form 4562, Depreciation and Amortization**  
Publication 536, NET OPERATING LOSSES  
**Form 1045, Application for Tentative Refund**  
Publication 537, INSTALLMENT SALES  
**Form 6252, Installment Sales**  
Publication 538, ACCOUNTING PERIODS AND METHODS  
Form 1128, Application to Adopt, Change or Retain a Tax Year  
Form 3115, Application for Change in Accounting Method  
Form 8716, Elections to Have a Tax Year Other Than a Required Tax Year  
Publication 541, PARTNERSHIPS  
**Form 1065 (Schedule K-1) U.S. Return of Partnership Income**  
Publication 542, CORPORATIONS  
**Forms 1120, 1120-A U. S. Corporation Income Tax Return**  
Publication 544, SALES AND OTHER DISPOSITIONS OF ASSETS  
**Form 1040 (Schedule D Capital Gains and Losses), Form 4797 Sale of Business Property, Form, 8824 Like-Kind Exchanges**  
Publication 547, CASUALTIES, DISASTERS AND THEFTS (BUSINESS & NON-BUSINESS)  
**Form 4684, Casualties and Thefts Section B-Business/Income Producing Property**  
Publication 551, BASIS OF ASSETS  
Publication 552, RECORDKEEPING FOR INDIVIDUALS  
Publication 553, HIGHLIGHTS OF 2001 TAX CHANGES  
Publication 556, EXAMINATION OF RETURNS, APPEAL RIGHTS AND CLAIMS FOR REFUND  
Publication 557, TAX-EXEMPT STATUS FOR YOUR ORGANIZATIONS  
**Forms 990, 990-EZ, 990-PF (Returns of Organization Exempt from Tax), Packages 1023, 1024 (Recognition of Exemption under Section 501 (c) (3) or 501 (a))**  
Publication 560, RETIREMENT PLANS FOR SMALL BUSINESS  
**Forms 5305-SEP, 5304-SIMPLE, 5305-SIMPLE and 5500EZ**  
Publication 564, MUTUAL FUND DISTRIBUTIONS  
**Forms 1040, (Schedules B Interest/Dividend Income, D Capital Gains (Sales), 1099-DIV Dividends and Distributions**  
Publication 575, PENSION AND ANNUITY INCOME

**Forms 1040, 1040A, 1099-R Distributions – Pensions/Annuities/Profit Sharing/IRAs, 4972 Tax on Lump Sum Distributions**

Publication 583, STARTING A BUSINESS AND KEEPING RECORDS

Publication 587, BUSINESS USE OF YOUR HOME

(INCLUDING USE BY DAY-CARE PROVIDERS)

**Form 8829 Business Use of Home (INCLUDING USE BY DAY-CARE PROVIDERS)**

Publication 590, INDIVIDUAL RETIREMENT ARRANGEMENTS (IRAs)

(INCLUDING ROTH IRAs AND EDUCATION IRAs)

**Forms 1040, 1040A, 1099-R Distributions – Pensions/Annuities/Profit Sharing/IRAs,, 5329 Additional Taxes on Qualified Plans, 8606 Nondeductible IRAs**

Publication 594, THE IRS COLLECTION PROCESS

Publication 595, TAX HIGHLIGHTS FOR COMMERCIAL FISHERMEN

**Forms 1040 (Schedule C), 1099-MISC Miscellaneous Income**

Publication 598, TAX ON UNRELATED BUSINESS INCOME OF

EXEMPT ORGANIZATIONS

**Form 990-T Exempt Organization – Business Income Tax Return**

Publication 908, BANKRUPTCY TAX GUIDE

**Forms 982, Reduction of Tax Attributes Due to Discharge of Indebtedness... 1040 U.S. Individual Income Tax Return, 1041 U.S. Income Tax Return for Estates and Trusts**

Publication 910, GUIDE TO FREE TAX SERVICES

Publication 911, DIRECT SELLERS

**Form 1040 (Schedules C Profits and Loss from Business, SE Self Employment Tax)**

Publication 925, PASSIVE ACTIVITY AND AT-RISK RULES

**Form 8582, Passive Activity Loss Limitations**

Publication 939, GENERAL RULE FOR PENSIONS AND ANNUITIES

Publication 946, HOW TO DEPRECIATE PROPERTY

**Form 4562, Depreciation and Amortization**

Publication 947, PRACTICE BEFORE THE IRS AND POWER OF ATTORNEY

**Forms 2848, Power of Attorney and Declaration of Representative, 8821 Tax Information Authorization**

Publication 1244, Employees Daily Record of Tips and Report to Employer contains

**Forms 4070, 4070-A**

Publication 1518, TAX CALENDAR FOR SMALL BUSINESS

Publication 1542, PER DIEM RATES

Publication 1544, REPORTING CASH PAYMENTS OF OVER \$10,00

(RECEIVED IN A TRADE OR BUSINESS)

**Form 8300, Report of Cash Payments Over \$10, 000 Received in Trade or Business**

Publication 1546, THE TAXPAYER ADVOCATE SERVICE OF THE IRS



Publication 1853, BUSINESS TALK  
Publication 3991, Highlights of Job Creation and Worker  
Assistance Act of 2002

# Lesson 2

## Employment Taxes

### Introduction

This lesson introduces federal employment taxes. It briefly explains your responsibilities as an employer to withhold and pay these taxes, and it gives other related information.

Employment taxes represent the income tax and social security and Medicare taxes (FICA taxes) withheld from the wages of an employee plus the employer's share of social security taxes and employer paid federal unemployment (FUTA) taxes. The withheld (employee's) portions of employment taxes are referred to as "trust fund" taxes.



### Objectives

At the end of this lesson you will be able to:

1. Determine an employer's responsibility for income tax withholding, social security and Medicare (FICA) taxes and federal unemployment (FUTA) taxes.
2. Determine the need for various forms related to employment taxes.
3. Determine the need for forms related to non-employee/ miscellaneous payments.

## Employer Identification Number (EIN)

When you start or buy a business, you may need to apply for an EIN to identify the tax returns of your business. If you don't already have an EIN, you need to get one if you:

- pay wages to employees,
- are required to withhold taxes for nonwage payments,
- have a self-employed retirement plan,
- operate your business as a corporation, partnership or
- are required to file any of these tax returns:
  - employment,
  - excise,
  - fiduciary or
  - alcohol, tobacco and firearms.



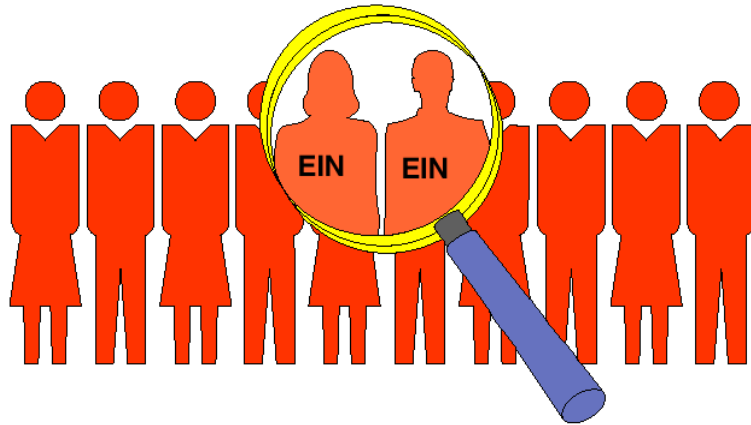
*Note: If you are a sole proprietor with no employees and don't meet any of the listed filing requirements, you do not need an EIN. If you need a number solely to identify your business's bank account, do not apply for an EIN but use your social security number (SSN) instead. This will save both you and the IRS paperwork and unnecessary correspondence.*

### Form SS-4

If you have not applied for an EIN and you are required to have one, you should obtain Form SS-4, APPLICATION FOR EMPLOYER IDENTIFICATION NUMBER, from the IRS. (See Exhibit 2.1.) The completed application should be mailed to the Internal Revenue Service Campus where you file your federal tax returns.

Fill out the SS-4 with the information requested in each box that applies.

Use your EIN on all the items you send to the IRS and Social Security Administration (SSA).



You should have only one EIN for yourself as a sole proprietor. For example, if you operate more than one sole proprietorship, you must use the same number for each. If you take over another employer's sole proprietorship, do not use that employer's EIN. If you have an EIN, use it. If not, apply for one.

Once you have received an EIN, you use it from one year to the next. If you change your business from a sole proprietorship, for example, to a corporation or partnership, apply for a new EIN. If you haven't received your number by the time a return is due, write "Applied for" and the date applied for in the EIN space.

***Note: Each separate partnership and corporation must have its own EIN.***

Apply for your EIN well before your tax returns are due to allow for IRS processing time. You may be able to obtain an EIN sooner by telephone or fax. See the instructions for Form SS-4 and Publication 1635, UNDERSTANDING YOUR EIN, for more information.

EXHIBIT 2.1 - BLANK FORM SS-4

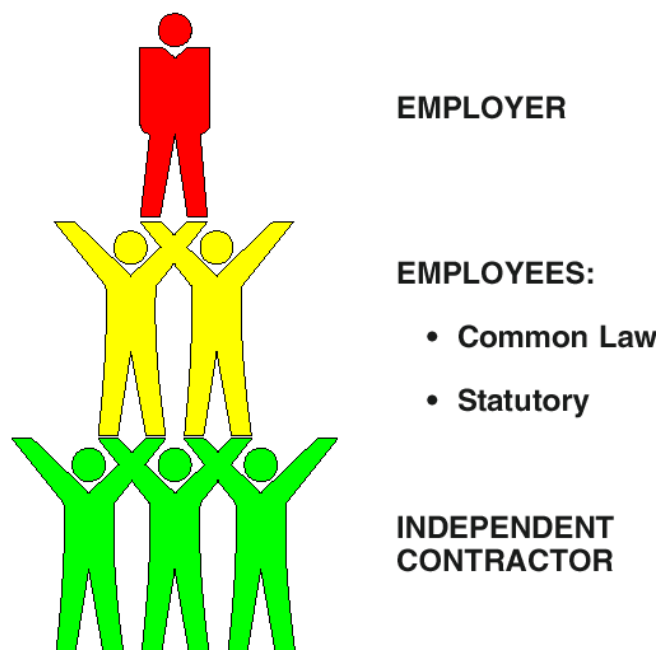
Form <b>SS-4</b> (Rev. December 2001) Department of the Treasury Internal Revenue Service	<b>Application for Employer Identification Number</b> (For use by employers, corporations, partnerships, trusts, estates, churches, government agencies, Indian tribal entities, certain individuals, and others.) ▶ See separate instructions for each line. ▶ Keep a copy for your records.	EIN _____  OMB No. 1545-0003														
Type or print clearly.	<b>1</b> Legal name of entity (or individual) for whom the EIN is being requested															
	<b>2</b> Trade name of business (if different from name on line 1)	<b>3</b> Executor, trustee, "care of" name														
	<b>4a</b> Mailing address (room, apt., suite no. and street, or P.O. box)	<b>5a</b> Street address (if different) (Do not enter a P.O. box.)														
	<b>4b</b> City, state, and ZIP code	<b>5b</b> City, state, and ZIP code														
	<b>6</b> County and state where principal business is located															
	<b>7a</b> Name of principal officer, general partner, grantor, owner, or trustor	<b>7b</b> SSN, ITIN, or EIN														
<b>8a Type of entity</b> (check only one box) <table style="width:100%; border: none;"> <tr> <td><input type="checkbox"/> Sole proprietor (SSN) _____</td> <td><input type="checkbox"/> Estate (SSN of decedent) _____</td> </tr> <tr> <td><input type="checkbox"/> Partnership</td> <td><input type="checkbox"/> Plan administrator (SSN) _____</td> </tr> <tr> <td><input type="checkbox"/> Corporation (enter form number to be filed) ▶ _____</td> <td><input type="checkbox"/> Trust (SSN of grantor) _____</td> </tr> <tr> <td><input type="checkbox"/> Personal service corp.</td> <td><input type="checkbox"/> National Guard <input type="checkbox"/> State/local government</td> </tr> <tr> <td><input type="checkbox"/> Church or church-controlled organization</td> <td><input type="checkbox"/> Farmers' cooperative <input type="checkbox"/> Federal government/military</td> </tr> <tr> <td><input type="checkbox"/> Other nonprofit organization (specify) ▶ _____</td> <td><input type="checkbox"/> REMIC <input type="checkbox"/> Indian tribal governments/enterprises</td> </tr> <tr> <td><input type="checkbox"/> Other (specify) ▶ _____</td> <td><input type="checkbox"/> Group Exemption Number (GEN) ▶ _____</td> </tr> </table>			<input type="checkbox"/> Sole proprietor (SSN) _____	<input type="checkbox"/> Estate (SSN of decedent) _____	<input type="checkbox"/> Partnership	<input type="checkbox"/> Plan administrator (SSN) _____	<input type="checkbox"/> Corporation (enter form number to be filed) ▶ _____	<input type="checkbox"/> Trust (SSN of grantor) _____	<input type="checkbox"/> Personal service corp.	<input type="checkbox"/> National Guard <input type="checkbox"/> State/local government	<input type="checkbox"/> Church or church-controlled organization	<input type="checkbox"/> Farmers' cooperative <input type="checkbox"/> Federal government/military	<input type="checkbox"/> Other nonprofit organization (specify) ▶ _____	<input type="checkbox"/> REMIC <input type="checkbox"/> Indian tribal governments/enterprises	<input type="checkbox"/> Other (specify) ▶ _____	<input type="checkbox"/> Group Exemption Number (GEN) ▶ _____
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<b>8b</b> If a corporation, name the state or foreign country (if applicable) where incorporated <table style="width:100%; border: none;"> <tr> <td style="border: none;">State</td> <td style="border: none;">Foreign country</td> </tr> </table>			State	Foreign country												
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<b>9 Reason for applying</b> (check only one box) <table style="width:100%; border: none;"> <tr> <td><input type="checkbox"/> Started new business (specify type) ▶ _____</td> <td><input type="checkbox"/> Banking purpose (specify purpose) ▶ _____</td> </tr> <tr> <td><input type="checkbox"/> Hired employees (Check the box and see line 12.)</td> <td><input type="checkbox"/> Changed type of organization (specify new type) ▶ _____</td> </tr> <tr> <td><input type="checkbox"/> Compliance with IRS withholding regulations</td> <td><input type="checkbox"/> Purchased going business</td> </tr> <tr> <td><input type="checkbox"/> Other (specify) ▶ _____</td> <td><input type="checkbox"/> Created a trust (specify type) ▶ _____</td> </tr> <tr> <td></td> <td><input type="checkbox"/> Created a pension plan (specify type) ▶ _____</td> </tr> </table>			<input type="checkbox"/> Started new business (specify type) ▶ _____	<input type="checkbox"/> Banking purpose (specify purpose) ▶ _____	<input type="checkbox"/> Hired employees (Check the box and see line 12.)	<input type="checkbox"/> Changed type of organization (specify new type) ▶ _____	<input type="checkbox"/> Compliance with IRS withholding regulations	<input type="checkbox"/> Purchased going business	<input type="checkbox"/> Other (specify) ▶ _____	<input type="checkbox"/> Created a trust (specify type) ▶ _____		<input type="checkbox"/> Created a pension plan (specify type) ▶ _____				
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<input type="checkbox"/> Compliance with IRS withholding regulations	<input type="checkbox"/> Purchased going business															
<input type="checkbox"/> Other (specify) ▶ _____	<input type="checkbox"/> Created a trust (specify type) ▶ _____															
	<input type="checkbox"/> Created a pension plan (specify type) ▶ _____															
<b>10</b> Date business started or acquired (month, day, year)		<b>11</b> Closing month of accounting year														
<b>12</b> First date wages or annuities were paid or will be paid (month, day, year). <b>Note:</b> If applicant is a withholding agent, enter date income will first be paid to nonresident alien. (month, day, year) . . . . .																
<b>13</b> Highest number of employees expected in the next 12 months. <b>Note:</b> If the applicant does not expect to have any employees during the period, enter "-0-". . . . . <table style="width:100%; border: none; margin-left: 20px;"> <tr> <td style="border: none; width: 33%;">Agricultural</td> <td style="border: none; width: 33%;">Household</td> <td style="border: none; width: 33%;">Other</td> </tr> </table>			Agricultural	Household	Other											
Agricultural	Household	Other														
<b>14</b> Check <b>one</b> box that best describes the principal activity of your business. <table style="width:100%; border: none; margin-left: 20px;"> <tr> <td><input type="checkbox"/> Construction</td> <td><input type="checkbox"/> Rental &amp; leasing</td> <td><input type="checkbox"/> Transportation &amp; warehousing</td> <td><input type="checkbox"/> Health care &amp; social assistance</td> <td><input type="checkbox"/> Accommodation &amp; food service</td> <td><input type="checkbox"/> Wholesale-agent/broker</td> </tr> <tr> <td><input type="checkbox"/> Real estate</td> <td><input type="checkbox"/> Manufacturing</td> <td><input type="checkbox"/> Finance &amp; insurance</td> <td><input type="checkbox"/> Other (specify)</td> <td><input type="checkbox"/> Wholesale-other</td> <td><input type="checkbox"/> Retail</td> </tr> </table>			<input type="checkbox"/> Construction	<input type="checkbox"/> Rental & leasing	<input type="checkbox"/> Transportation & warehousing	<input type="checkbox"/> Health care & social assistance	<input type="checkbox"/> Accommodation & food service	<input type="checkbox"/> Wholesale-agent/broker	<input type="checkbox"/> Real estate	<input type="checkbox"/> Manufacturing	<input type="checkbox"/> Finance & insurance	<input type="checkbox"/> Other (specify)	<input type="checkbox"/> Wholesale-other	<input type="checkbox"/> Retail		
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<b>15</b> Indicate principal line of merchandise sold; specific construction work done; products produced; or services provided.																
<b>16a</b> Has the applicant ever applied for an employer identification number for this or any other business? . . . . . <input type="checkbox"/> <b>Yes</b> <input type="checkbox"/> <b>No</b> <b>Note:</b> If "Yes," please complete lines 16b and 16c.																
<b>16b</b> If you checked "Yes" on line 16a, give applicant's legal name and trade name shown on prior application if different from line 1 or 2 above. Legal name ▶ _____ Trade name ▶ _____																
<b>16c</b> Approximate date when, and city and state where, the application was filed. Enter previous employer identification number if known. Approximate date when filed (mo., day, year) _____ City and state where filed _____ Previous EIN _____																
Third Party Designee	Complete this section <b>only</b> if you want to authorize the named individual to receive the entity's EIN and answer questions about the completion of this form.															
	Designee's name	Designee's telephone number (include area code) ( )														
	Address and ZIP code	Designee's fax number (include area code) ( )														
Under penalties of perjury, I declare that I have examined this application, and to the best of my knowledge and belief, it is true, correct, and complete.		Applicant's telephone number (include area code) ( )														
Name and title (type or print clearly) ▶ _____		Applicant's fax number (include area code) ( )														
Signature ▶ _____	Date ▶ _____															
For Privacy Act and Paperwork Reduction Act Notice, see separate instructions. <span style="float: right;">Cat. No. 16055N Form <b>SS-4</b> (Rev. 12-2001)</span>																

## Employer/Employees

It is important to know whether you are considered an employer for tax purposes. A person or organization may be an employer for purposes of one kind of tax but not for another. A person who works for you may be classified as a common-law employee, a statutory employee or an independent contractor. The classification of the person determines which forms you must file, which taxes you must pay and deposit requirements. For more information on these classifications, see Publication 15-A, EMPLOYER'S SUPPLEMENTAL TAX GUIDE.

Generally, anyone who performs services for you is your employee if you can control what will be done and how it will be done. This is so even when you give the employee freedom of action. What matters is that you have the right to control the details of how the services are performed. Publication 15-A has more information on how to determine whether an individual providing services is an independent contractor or an employee.

To get a determination from the IRS as to whether or not a worker is an employee, file Form SS-8, DETERMINATION OF EMPLOYEE WORK STATUS FOR PURPOSES OF FEDERAL EMPLOYMENT TAXES AND INCOME TAX WITHHOLDING.



**Independent  
Contractors**

An *independent contractor* performs services for you, but is not under your direct control. Generally, people in business for themselves are not employees. For example, doctors, lawyers, veterinarians, construction contractors and others in an independent trade in which they offer their services to the public are usually not employees. However, whether such people are employees or independent contractors depends on the facts in each case. The general rule is that an individual is an independent contractor if you, the employer, have the right to control or direct only the result of the work and not the means and methods of accomplishing the result.

See Publication 15-A for more information.

## Form W-4

To know how much federal income tax to withhold from an employee's wages, you should have a Form W-4, EMPLOYEE'S WITHHOLDING ALLOWANCE CERTIFICATE, on file for each employee. The amount to be withheld is determined by the employee's gross wages and the information submitted by the employee on Form W-4. (See Exhibit 2.2.)

This information includes:

- employee's marital status;
- number of withholding allowances claimed;
- employee's request to have additional tax withheld or
- employee's claim to exemption from withholding.

Ask each new employee to give you a signed Form W-4 by his or her first day of work. This certificate is effective with the first wage payment and will last until the employee files a new certificate.

If an employee does not give you a Form W-4, withhold tax as if the employee were a single person who has claimed no withholding allowances. If not enough tax is withheld and your employee has not provided a Form W-4 or has claimed an Exemption from withholding, he or she may be subject to penalties. An employee who claims exemption from withholding must renew his or her status by filing a new Form W-4 with you by February 15 of each year.

**Note: Student status does not automatically exempt the employee from income tax withholding.**

Generally, Forms W-4 are for your records. They need not be sent to IRS unless:

- the employee claims more than 10 withholding allowances  
or
- the employee normally earns more than \$200 per week and claims *exemption from withholding* on Line 7.

For more information on withholding, see Publication 505, TAX WITHHOLDING AND ESTIMATED TAX. You can help your employees determine whether they are having the right amount of income tax withheld by ordering copies of Publication 919, HOW DO I ADJUST MY TAX WITHHOLDING?



EXHIBIT 2.2 - BLANK FORM W-4, PAGE 1

**Form W-4 (2002)**

**Purpose.** Complete Form W-4 so your employer can withhold the correct Federal income tax from your pay. Because your tax situation may change, you may want to refigure your withholding each year.

**Exemption from withholding.** If you are exempt, complete only lines 1, 2, 3, 4, and 7 and sign the form to validate it. Your exemption for 2002 expires February 16, 2003. See **Pub. 505**, Tax Withholding and Estimated Tax.

**Note:** You cannot claim exemption from withholding if (a) your income exceeds \$750 and includes more than \$250 of unearned income (e.g., interest and dividends) and (b) another person can claim you as a dependent on their tax return.

**Basic instructions.** If you are not exempt, complete the **Personal Allowances Worksheet** below. The worksheets on page 2 adjust your withholding allowances based on itemized deductions, certain credits, adjustments to

income, or two-earner/two-job situations. Complete all worksheets that apply. **However, you may claim fewer (or zero) allowances.**

**Head of household.** Generally, you may claim head of household filing status on your tax return only if you are unmarried and pay more than 50% of the costs of keeping up a home for yourself and your dependent(s) or other qualifying individuals. See line E below.

**Tax credits.** You can take projected tax credits into account in figuring your allowable number of withholding allowances. Credits for child or dependent care expenses and the child tax credit may be claimed using the **Personal Allowances Worksheet** below. See **Pub. 919**, How Do I Adjust My Tax Withholding? for information on converting your other credits into withholding allowances.

**Nonwage income.** If you have a large amount of nonwage income, such as interest or dividends, consider making estimated tax payments using **Form 1040-ES**, Estimated Tax for Individuals. Otherwise, you may owe additional tax.

**Two earners/two jobs.** If you have a working spouse or more than one job, figure the total number of allowances you are entitled to claim on all jobs using worksheets from only one Form W-4. Your withholding usually will be most accurate when all allowances are claimed on the Form W-4 for the highest paying job and zero allowances are claimed on the others.

**Nonresident alien.** If you are a nonresident alien, see the **Instructions for Form 8233** before completing this Form W-4.

**Check your withholding.** After your Form W-4 takes effect, use **Pub. 919** to see how the dollar amount you are having withheld compares to your projected total tax for 2002. See **Pub. 919**, especially if you used the **Two-Earner/Two-Job Worksheet** on page 2 and your earnings exceed \$125,000 (Single) or \$175,000 (Married).

**Recent name change?** If your name on line 1 differs from that shown on your social security card, call 1-800-772-1213 for a new social security card.

**Personal Allowances Worksheet** (Keep for your records.)

**A** Enter "1" for yourself if no one else can claim you as a dependent . . . . . **A** \_\_\_\_\_

**B** Enter "1" if:   
 { • You are single and have only one job; or   
 • You are married, have only one job, and your spouse does not work; or   
 • Your wages from a second job or your spouse's wages (or the total of both) are \$1,000 or less. } . . . **B** \_\_\_\_\_

**C** Enter "1" for your spouse. But, you may choose to enter "-0-" if you are married and have either a working spouse or more than one job. (Entering "-0-" may help you avoid having too little tax withheld.) . . . . . **C** \_\_\_\_\_

**D** Enter number of dependents (other than your spouse or yourself) you will claim on your tax return . . . . . **D** \_\_\_\_\_

**E** Enter "1" if you will file as head of household on your tax return (see conditions under **Head of household** above) . . . **E** \_\_\_\_\_

**F** Enter "1" if you have at least \$1,500 of child or dependent care expenses for which you plan to claim a credit . . . **F** \_\_\_\_\_

**(Note: Do not include child support payments. See Pub. 503, Child and Dependent Care Expenses, for details.)**

**G Child Tax Credit** (including additional child tax credit):   
 • If your total income will be between \$15,000 and \$42,000 (\$20,000 and \$65,000 if married), enter "1" for each eligible child plus 1 additional if you have three to five eligible children or 2 additional if you have six or more eligible children.   
 • If your total income will be between \$42,000 and \$80,000 (\$65,000 and \$115,000 if married), enter "1" if you have one or two eligible children, "2" if you have three eligible children, "3" if you have four eligible children, or "4" if you have five or more eligible children. **G** \_\_\_\_\_

**H** Add lines A through G and enter total here. **Note:** This may be different from the number of exemptions you claim on your tax return. **H** \_\_\_\_\_

For accuracy, complete all worksheets that apply.   
 { • If you plan to itemize or claim adjustments to income and want to reduce your withholding, see the **Deductions and Adjustments Worksheet** on page 2.   
 • If you have more than one job or are married and you and your spouse both work and the combined earnings from all jobs exceed \$35,000, see the **Two-Earner/Two-Job Worksheet** on page 2 to avoid having too little tax withheld.   
 • If neither of the above situations applies, stop here and enter the number from line H on line 5 of Form W-4 below.

Cut here and give Form W-4 to your employer. Keep the top part for your records.

Form <b>W-4</b> Department of the Treasury Internal Revenue Service		<b>Employee's Withholding Allowance Certificate</b>	OMB No. 1545-0010 <b>2002</b>
1 Type or print your first name and middle initial Last name		2 Your social security number	
Home address (number and street or rural route)		3 <input type="checkbox"/> Single <input type="checkbox"/> Married <input type="checkbox"/> Married, but withhold at higher Single rate. <small>Note: If married, but legally separated, or spouse is a nonresident alien, check the "Single" box.</small>	
City or town, state, and ZIP code		4 If your last name differs from that on your social security card, check here. You must call 1-800-772-1213 for a new card. <input type="checkbox"/>	
5 Total number of allowances you are claiming (from line H above or from the applicable worksheet on page 2)		5 _____	
6 Additional amount, if any, you want withheld from each paycheck		6 \$ _____	
7 I claim exemption from withholding for 2002, and I certify that I meet both of the following conditions for exemption: • Last year I had a right to a refund of all Federal income tax withheld because I had no tax liability and • This year I expect a refund of all Federal income tax withheld because I expect to have no tax liability. If you meet both conditions, write "Exempt" here		7 _____	
Under penalties of perjury, I certify that I am entitled to the number of withholding allowances claimed on this certificate, or I am entitled to claim exempt status.			
<b>Employee's signature</b> (Form is not valid unless you sign it.)			
8 Employer's name and address (Employer: Complete lines 8 and 10 only if sending to the IRS.)		Date	
9 Office code (optional)		10 Employer identification number	

EXHIBIT 2.2 - BLANK FORM W-4, PAGE 2

**Deductions and Adjustments Worksheet**

**Note:** Use this worksheet only if you plan to itemize deductions, claim certain credits, or claim adjustments to income on your 2002 tax return.

**1** Enter an estimate of your 2002 itemized deductions. These include qualifying home mortgage interest, charitable contributions, state and local taxes, medical expenses in excess of 7.5% of your income, and miscellaneous deductions. (For 2002, you may have to reduce your itemized deductions if your income is over \$137,300 (\$68,650 if married filing separately). See **Worksheet 3** in Pub. 919 for details.) **1** \$ \_\_\_\_\_

**2** Enter:  $\left\{ \begin{array}{l} \$7,850 \text{ if married filing jointly or qualifying widow(er)} \\ \$6,900 \text{ if head of household} \\ \$4,700 \text{ if single} \\ \$3,925 \text{ if married filing separately} \end{array} \right\}$  **2** \$ \_\_\_\_\_

**3** Subtract line 2 from line 1. If line 2 is greater than line 1, enter "-0-". **3** \$ \_\_\_\_\_

**4** Enter an estimate of your 2002 adjustments to income, including alimony, deductible IRA contributions, and student loan interest. **4** \$ \_\_\_\_\_

**5** Add lines 3 and 4 and enter the total. Include any amount for credits from **Worksheet 7** in Pub. 919. **5** \$ \_\_\_\_\_

**6** Enter an estimate of your 2002 nonwage income (such as dividends or interest). **6** \$ \_\_\_\_\_

**7** Subtract line 6 from line 5. Enter the result, but not less than "-0-". **7** \$ \_\_\_\_\_

**8** Divide the amount on line 7 by \$3,000 and enter the result here. Drop any fraction. **8** \_\_\_\_\_

**9** Enter the number from the **Personal Allowances Worksheet**, line H, page 1. **9** \_\_\_\_\_

**10** Add lines 8 and 9 and enter the total here. If you plan to use the **Two-Earner/Two-Job Worksheet**, also enter this total on line 1 below. Otherwise, **stop here** and enter this total on Form W-4, line 5, page 1. **10** \_\_\_\_\_

**Two-Earner/Two-Job Worksheet**

**Note:** Use this worksheet only if the instructions under line H on page 1 direct you here.

**1** Enter the number from line H, page 1 (or from line 10 above if you used the **Deductions and Adjustments Worksheet**) **1** \_\_\_\_\_

**2** Find the number in **Table 1** below that applies to the **lowest** paying job and enter it here. **2** \_\_\_\_\_

**3** If line 1 is **more than or equal to** line 2, subtract line 2 from line 1. Enter the result here (if zero, enter "-0-") and on Form W-4, line 5, page 1. **Do not** use the rest of this worksheet. **3** \_\_\_\_\_

**Note:** If line 1 is **less than** line 2, enter "-0-" on Form W-4, line 5, page 1. Complete lines 4-9 below to calculate the additional withholding amount necessary to avoid a year end tax bill.

**4** Enter the number from line 2 of this worksheet. **4** \_\_\_\_\_

**5** Enter the number from line 1 of this worksheet. **5** \_\_\_\_\_

**6** Subtract line 5 from line 4. **6** \_\_\_\_\_

**7** Find the amount in **Table 2** below that applies to the **highest** paying job and enter it here. **7** \$ \_\_\_\_\_

**8** Multiply line 7 by line 6 and enter the result here. This is the additional annual withholding needed. **8** \$ \_\_\_\_\_

**9** Divide line 8 by the number of pay periods remaining in 2002. For example, divide by 26 if you are paid every two weeks and you complete this form in December 2001. Enter the result here and on Form W-4, line 6, page 1. This is the additional amount to be withheld from each paycheck. **9** \$ \_\_\_\_\_

**Table 1: Two-Earner/Two-Job Worksheet**

Married Filing Jointly				All Others			
If wages from LOWEST paying job are—	Enter on line 2 above	If wages from LOWEST paying job are—	Enter on line 2 above	If wages from LOWEST paying job are—	Enter on line 2 above	If wages from LOWEST paying job are—	Enter on line 2 above
\$0 - \$4,000	0	44,001 - 50,000	8	\$0 - \$6,000	0	75,001 - 95,000	8
4,001 - 9,000	1	50,001 - 55,000	9	6,001 - 11,000	1	95,001 - 110,000	9
9,001 - 15,000	2	55,001 - 65,000	10	11,001 - 17,000	2	110,001 and over	10
15,001 - 20,000	3	65,001 - 80,000	11	17,001 - 23,000	3		
20,001 - 25,000	4	80,001 - 95,000	12	23,001 - 28,000	4		
25,001 - 32,000	5	95,001 - 110,000	13	28,001 - 38,000	5		
32,001 - 38,000	6	110,001 - 125,000	14	38,001 - 55,000	6		
38,001 - 44,000	7	125,001 and over	15	55,001 - 75,000	7		

**Table 2: Two-Earner/Two-Job Worksheet**

Married Filing Jointly		All Others	
If wages from HIGHEST paying job are—	Enter on line 7 above	If wages from HIGHEST paying job are—	Enter on line 7 above
\$0 - \$50,000	\$450	\$0 - \$30,000	\$450
50,001 - 100,000	800	30,001 - 70,000	800
100,001 - 150,000	900	70,001 - 140,000	900
150,001 - 270,000	1,050	140,001 - 300,000	1,050
270,001 and over	1,150	300,001 and over	1,150

**Privacy Act and Paperwork Reduction Act Notice.** We ask for the information on this form to carry out the Internal Revenue laws of the United States. The Internal Revenue Code requires this information under sections 3402(f)(2)(A) and 6109 and their regulations. **Failure to provide a properly completed form will result in your being treated as a single person who claims no withholding allowances; providing fraudulent information may also subject you to penalties.** Routine uses of this information include giving it to the Department of Justice for civil and criminal litigation, to cities, states, and the District of Columbia for use in administering their tax laws, and using it in the National Directory of New Hires.

control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Code section 6103.

The time needed to complete this form will vary depending on individual circumstances. The estimated average time is: **Recordkeeping**, 46 min.; **Learning about the law or the form**, 13 min.; **Preparing the form**, 59 min. If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write to the Tax Forms Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. **Do not** send the tax form to this address. Instead, give it to your employer.



# Form I-9

All U.S. employers must verify the employment and identity of all employees hired to work in the United States. Both you and the employee must complete the Immigration and Naturalization Service (INS) Form I-9, EMPLOYMENT ELIGIBILITY VERIFICATION. (See Exhibit 2.3.) Employers must maintain completed I-9s in their own files for three (3) years after the date of hire or one (1) year after the date employment ends, whichever is later. You can get the form from INS offices, by calling **1-800-829-3676** or by visiting the INS Web site at [www.ins.usdoj.gov](http://www.ins.usdoj.gov). Call the INS at **1-800-375-5283** for more information about your responsibilities.

## EXHIBIT 2.3 - BLANK FORM I-9

U.S. Department of Justice Immigration and Naturalization Service		OMB No. 1115-0136	
		<b>Employment Eligibility Verification</b>	
Please read instructions carefully before completing this form. The instructions must be available during completion of this form. <b>ANTI-DISCRIMINATION NOTICE:</b> It is illegal to discriminate against work eligible individuals. Employers CANNOT specify which document(s) they will accept from an employee. The refusal to hire an individual because of a future expiration date may also constitute illegal discrimination.			
<b>Section 1. Employee Information and Verification.</b> To be completed and signed by employee at the time employment begins.			
Print Name: Last		First	Middle Initial
			Maiden Name:
Address (Street Name and Number)		Apt. #	Date of Birth (month/day/year)
City	State	Zip Code	Social Security #
I am aware that federal law provides for imprisonment and/or fines for false statements or use of false documents in connection with the completion of this form.		I attest, under penalty of perjury, that I am (check one of the following):	
		<input type="checkbox"/> A citizen or national of the United States <input type="checkbox"/> A Lawful Permanent Resident (Alien # A _____) <input type="checkbox"/> An alien authorized to work until ___/___/___ (Alien # or Admission #)	
Employee's Signature		Date (month/day/year)	
<b>Preparer and/or Translator Certification.</b> (To be completed and signed if Section 1 is prepared by a person other than the employee.) I attest, under penalty of perjury, that I have assisted in the completion of this form and that to the best of my knowledge the information is true and correct.			
Preparer's/Translator's Signature		Print Name	
Address (Street Name and Number, City, State, Zip Code)		Date (month/day/year)	
<b>Section 2. Employer Review and Verification.</b> To be completed and signed by employer. Examine one document from List A OR examine one document from List B and one from List C, as listed on the reverse of this form, and record the title, number and expiration date, if any, of the document(s)			
List A	OR	List B	AND
List C			
Document title: _____		_____	_____
Issuing authority: _____		_____	_____
Document #: _____		_____	_____
Expiration Date (if any): ___/___/___		___/___/___	___/___/___
Document #: _____			
Expiration Date (if any): ___/___/___			
<b>CERTIFICATION - I attest, under penalty of perjury, that I have examined the document(s) presented by the above-named employee, that the above-listed document(s) appear to be genuine and to relate to the employee named, that the employee began employment on (month/day/year) ___/___/___ and that to the best of my knowledge the employee is eligible to work in the United States. (State employment agencies may omit the date the employee began employment.)</b>			
Signature of Employer or Authorized Representative		Print Name	Title
Business or Organization Name		Address (Street Name and Number, City, State, Zip Code)	Date (month/day/year)
<b>Section 3. Updating and Reverification.</b> To be completed and signed by employer.			
A. New Name (if applicable)		B. Date of rehire (month/day/year) (if applicable)	
C. If employee's previous grant of work authorization has expired, provide the information below for the document that establishes current employment eligibility.			
Document Title: _____	Document #: _____	Expiration Date (if any): ___/___/___	
I attest, under penalty of perjury, that to the best of my knowledge, this employee is eligible to work in the United States, and if the employee presented document(s), the document(s) I have examined appear to be genuine and to relate to the individual.			
Signature of Employer or Authorized Representative		Date (month/day/year)	

# Information Returns

## Form 1099-MISC

You do not withhold income tax or social security and Medicare taxes from, or pay social security and Medicare taxes or federal unemployment tax on amounts you pay an independent contractor/nonemployee. Generally, if you pay at least \$600 during the year to an independent contractor/nonemployee for services (including parts and materials) performed in the course of your business, you must furnish a Form 1099-MISC (Miscellaneous Income) to that person by January 31 of the following year. (See Exhibit 2.4.).

You will need the social security number or EIN of an independent contractor in order to complete Form 1099-MISC. If the independent contractor is a sole proprietor, their SSN is preferred. Always ask the independent contractor to complete Form W-9, REQUEST FOR TAXPAYER IDENTIFICATION NUMBER AND CERTIFICATION, before beginning work. (See Exhibit 2.5.) If you do not obtain an SSN or EIN before you pay the contractor, you must withhold income tax from the payment. This is called *backup withholding*. Backup withholding rules require that 30% of the payment be withheld. Report the backup withholding on Form 945, ANNUAL RETURN OF WITHHELD FEDERAL INCOME TAX, discussed in Lesson 3.

**EXHIBIT 2.4 - BLANK FORM 1099-MISC**

9595 <input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		OMB No. 1545-0115		<b>Miscellaneous Income</b>
PAYER'S name, street address, city, state, ZIP code, and telephone no.		1 Rents	<b>2002</b>	
		\$		2 Royalties
PAYER'S Federal identification number		\$	3 Other income	4 Federal income tax withheld
		\$	\$	5 Fishing boat proceeds
RECIPIENT'S identification number		\$	6 Medical and health care payments	<b>Copy A For Internal Revenue Service Center</b>
RECIPIENT'S name		\$	7 Nonemployee compensation	
Street address (including apt. no.)		\$	8 Substitute payments in lieu of dividends or interest	<b>For Privacy Act and Paperwork Reduction Act Notice, see the 2002 General Instructions for Forms 1099, 1098, 5498, and W-2G.</b>
City, state, and ZIP code		\$	9 Payer made direct sales of \$5,000 or more of consumer products to a buyer (recipient) for resale <input type="checkbox"/>	
Account number (optional)		\$	10 Crop insurance proceeds	<b>2002 General Instructions for Forms 1099, 1098, 5498, and W-2G.</b>
2nd TIN not <input type="checkbox"/>		\$	11	
15		\$	12	<b>Form 1099-MISC</b>
		\$	13 Excess golden parachute payments	
16 State tax withheld		\$	14 Gross proceeds paid to an attorney	<b>Department of the Treasury - Internal Revenue Service</b>
		\$	\$	
18 State income		\$	18 State income	<b>Do Not Cut or Separate Forms on This Page — Do Not Cut or Separate Forms on This Page</b>
		\$	\$	

**Note:** *Do not report payments to corporations on Form 1099-MISC unless you are reporting payments for medical, health or legal services. For additional information on 1099 reporting requirements refer to the Instructions for Forms 1099, 1098, 5498 and W2G.*

**EXHIBIT 2.5 - BLANK FORM W-9**

Form <b>W-9</b> (Rev. January 2002) Department of the Treasury Internal Revenue Service	<b>Request for Taxpayer                  Identification Number and Certification</b>	Give form to the requester. Do not send to the IRS.
Print or type See Specific Instructions on page 2.	Name	
	Business name, if different from above	
	Check appropriate box: <input type="checkbox"/> Individual/Sole proprietor <input type="checkbox"/> Corporation <input type="checkbox"/> Partnership <input type="checkbox"/> Other ..... <input type="checkbox"/> Exempt from backup withholding	
	Address (number, street, and apt. or suite no.)	Requester's name and address (optional)
	City, state, and ZIP code	
List account number(s) here (optional)		
<b>Part I Taxpayer Identification Number (TIN)</b>		
Enter your TIN in the appropriate box. For individuals, this is your social security number (SSN). However, for a resident alien, sole proprietor, or disregarded entity, see the Part I instructions on page 2. For other entities, it is your employer identification number (EIN). If you do not have a number, see How to get a TIN on page 2.		Social security number                 or Employer identification number 
Note: If the account is in more than one name, see the chart on page 2 for guidelines on whose number to enter.		
<b>Part II Certification</b>		
Under penalties of perjury, I certify that:		
1. The number shown on this form is my correct taxpayer identification number (or I am waiting for a number to be issued to me), and 2. I am not subject to backup withholding because: (a) I am exempt from backup withholding, or (b) I have not been notified by the Internal Revenue Service (IRS) that I am subject to backup withholding as a result of a failure to report all interest or dividends, or (c) the IRS has notified me that I am no longer subject to backup withholding, and 3. I am a U.S. person (including a U.S. resident alien).		
Certification instructions. You must cross out item 2 above if you have been notified by the IRS that you are currently subject to backup withholding because you have failed to report all interest and dividends on your tax return. For real estate transactions, item 2 does not apply. For mortgage interest paid, acquisition or abandonment of secured property, cancellation of debt, contributions to an individual retirement arrangement (IRA), and generally, payments other than interest and dividends, you are not required to sign the Certification, but you must provide your correct TIN. (See the instructions on page 2.)		
Sign Here	Signature of U.S. person ▶	Date ▶

**Form W-2**

You must furnish a copy of Form W-2, WAGE AND TAX STATEMENT, to each employee to whom you paid wages during the year. (See Exhibit 2.6.)

Form W-2 must show total wages and other compensation paid (even if not subject to withholding); total wages subject to social security and Medicare taxes; allocated tips (if any); amounts deducted for income, social security and Medicare taxes; and the total advance earned income credit payment (discussed later). In all cases, you must give each of your employees the statement by

January 31 following the end of the calendar year covered. If not computer-generated, every effort should be made to ensure that Forms W-2 provided to employees are legible.

If employment ends before the close of the year, the employee may request the form earlier. You must give the employee a Form W-2 within 30 days of the employee’s request or within 30 days of the final wage payment, whichever is later.

You should keep any undeliverable employee copies of Form W-2 (Copies B and C) as part of your records for 4 years.

**EXHIBIT 2.6 - BLANK FORM W-2**

a Control number		22222		Void <input type="checkbox"/>		For Official Use Only ▶ OMB No. 1545-0008	
b Employer identification number				1 Wages, tips, other compensation		2 Federal income tax withheld	
c Employer's name, address, and ZIP code				\$		\$	
				3 Social security wages		4 Social security tax withheld	
				\$		\$	
				5 Medicare wages and tips		6 Medicare tax withheld	
d Employee's social security number				7 Social security tips		8 Allocated tips	
e Employee's first name and initial				9 Advance EIC payment		10 Dependent care benefits	
				\$		\$	
Last name				11 Nonqualified plans		12a See instructions for box 12	
f Employee's address and ZIP code				\$		\$	
				13 Statutory employee <input type="checkbox"/> Retirement plan <input type="checkbox"/> Third party sick pay <input type="checkbox"/>		12b	
				14 Other		\$	
						\$	
15 State		Employer's state ID number		16 State wages, tips, etc.		17 State income tax	
\$				\$		\$	
				\$		\$	
				18 Local wages, tips, etc.		19 Local income tax	
				\$		\$	
						20 Locality name	

**W-2 Wage and Tax Statement** (99) **2002** Department of the Treasury—Internal Revenue Service  
 Copy A For Social Security Administration—Send this entire page with Form W-3 to the Social Security Administration; photocopies are not acceptable. (Rev. February 2002) For Privacy Act and Paperwork Reduction Act Notice, see separate instructions.  
 Cat. No. 10134D

**Do Not Cut, Fold, or Staple Forms on This Page — Do Not Cut, Fold, or Staple Forms on This Page**

## Income Tax

The wages you pay your employees generally are subject to income tax withholding if their wages for any payroll period are more than the dollar amount of their withholding allowances for that period. The amount to be withheld is figured separately for each payroll period. Wages include all pay you give an employee for services performed. The pay may be in cash or in other forms. It includes salaries, vacation allowances, bonuses, commissions and fringe benefits not excluded by law. It does not matter how payments are measured or paid. Wages paid in any form other than money (such as goods, lodging and meals) are measured by the fair market value. See Publication 15, *EMPLOYER'S TAX GUIDE (Circular E)* for more information about income tax withholding and requirements to deposit withheld taxes.

## Tipped Employees



Tips your employees receive are generally subject to withholding. Each employee who receives at least \$20 in tips in a month must report to you all tips they receive. This report must be made by the 10th day of each month following the month in which the tips are received. Tips that an employee receives directly from customers and tips that charge customers add to the bill and you pay to the employee must be reported. Your employee reports the tips on Form 4070, *EMPLOYEE'S REPORT ON TIPS TO EMPLOYER*, or a similar form. See Publication 1244, *EMPLOYEE'S DAILY RECORD OF TIPS AND REPORT OF TIPS TO EMPLOYER*, which includes Form 4070, for more information.

**Note: There are special tip reporting requirements for large food and beverage establishments. These businesses provide food and beverages for consumption on the premises, tipping is customary, and they usually employ more than 10 employees on a typical business day. These rules affect only the reporting requirements.**

## All Employees

The income tax to be withheld is figured on gross wages before any deductions are made for social security and Medicare taxes, pension, union dues, insurance, etc. You may figure the withholding by different methods, the most common of which are the percentage method and the wage bracket tables method. Publication 15 contains the applicable tables and instructions for using both of these withholding methods, and it gives more information on reporting and withholding requirements on wages and tip income.

## Social Security and Medicare Taxes

Under the Federal Insurance Contributions Act (FICA), you must withhold social security and Medicare taxes from wages that you pay your employees each payroll period.

Generally, meals, lodging, clothing, services and other payments in kind are subject to social security and Medicare taxes, as are wages paid in cash. However, meals are not taxable wages if furnished for the employer's convenience and on the employer's premises.

Lodging is not taxable if furnished for the employer's convenience, on the employer's premises and as a condition of employment.

You, as an employer, must withhold and deposit the employee's part of the taxes and pay a matching amount. The social security tax is withheld from the employee's gross wages until the employee's cumulative wages for the year reach the wage base limit. Any wages above the wage base limit are not subject to social security tax withholding. However, there is no wage base limit for Medicare tax; **all covered wages are subject to Medicare tax.**

For 2002, the limit for wages subject to social security tax is \$84,900. The social security tax rate is 6.2% for the employee and 6.2% for the employer (12.4% total). The Medicare tax rate for the employee is 1.45% and 1.45% for the employer (2.9% total). This means that in 2002 you are to withhold employee social security and Medicare taxes at the total rate of 7.65% (6.2% up to \$84,900 plus 1.45% for all wages) and pay, or deposit, 15.30% (the total of the employee share and the employer's matching share of 7.65%).

## Federal Unemployment Tax

The Federal Unemployment Tax Act (FUTA) provides for the states and the Federal Government to cooperate in establishing and administering an unemployment tax program. Most employers pay both a federal and a state unemployment tax. The federal unemployment program was enacted to encourage the states to provide payment to workers who have lost their jobs. Only the employer pays FUTA tax; it is not deducted from an employee's wages. For 2002, federal unemployment tax is figured on the first \$7,000 you pay to each employee during the year. See Publication 15 and the INSTRUCTIONS FOR FORM 940 for more information.



## Successor Employer

If you acquired all or substantially all of the property used in the business of another employer, you may, in figuring the wage limit for social security and federal unemployment tax purposes, include the wages that employer paid to the employees who continue to work for you.

## Earned Income Credit (EIC)



The EIC is a tax credit for certain workers whose earned income is below a certain level. Because it is a “credit,” the EIC is subtracted from the amount of tax owed. Even workers who have not filed a tax return in the previous year, because their wages were below the minimum income-level requirements to file, may be able to receive the credit — but only if they file a tax return. Therefore, you must notify each employee who worked for you at any time during the year, and from whom you did not withhold any income tax, about the EIC. You will meet the notification requirements by giving the employee either Notice 797, POSSIBLE REFUND ON YOUR FEDERAL INCOME TAX RETURNS BECAUSE OF THE EARNED INCOME CREDIT (EIC); your own written statement as long as it has the exact wording of Notice 797; or the official IRS Form W-2, WAGE AND TAX STATEMENT, which contains a statement on the back of Copy C. Exception: You do not need to notify those employees who claimed exemption from withholding on Form W-4, EMPLOYEE’S WITHHOLDING ALLOWANCE CERTIFICATE.

An employee who expects to earn less than \$29,201 in 2002 and has a qualifying child can receive advance payments of up to 60% of the maximum credit for one qualifying child. For 2002, this is \$1,503. To claim the advance EIC, eligible employees must provide you a properly completed Form W-5, EARNED INCOME CREDIT ADVANCE PAYMENT CERTIFICATE. (See Exhibit 2.7.) You use the advance EIC tables in Publication 15 each payroll period to figure the correct amount of advance payment to include in the employee’s pay. For depositing purposes, the advance payment first reduces the withheld income tax and then the employee and employer social security and Medicare taxes, thereby reducing your total tax liability.

**Reminder: Do not continue advance EIC payments to an employee on wages of less than \$29,201 (\$30,201 if married filing jointly) in 2002.**

For more information, see Publication 15.

**Note: In 2002, an employee’s advance EIC payments are limited to a total of \$1,503, although the credit may be more. They will have to claim any additional amount of EIC on their tax return.**

EXHIBIT 2.7 - BLANK FORM W-5

# 2002 Form W-5



## Instructions

### Changes To Note

Beginning in 2002, new rules apply to determine who is a qualifying child for purposes of the earned income credit (EIC). See page 2. Also, nontaxable earned income and modified adjusted gross income (MAGI) are no longer taken into account to determine who is eligible for the credit or the amount of the credit. Taxable earned income and AGI are used instead.

### Purpose

Use Form W-5 if you are eligible to get part of the EIC in advance with your pay and choose to do so. See **Who Is Eligible To Get Advance EIC Payments?** below. The amount you can get in advance generally depends on your wages. If you are married, the amount of your advance EIC payments also depends on whether your spouse has filed a Form W-5 with his or her employer. However, your employer cannot give you more than \$1,503 throughout 2002 with your pay. You will get the rest of any EIC you are entitled to when you file your tax return and claim the EIC.

If you do not choose to get advance payments, you can still claim the EIC on your 2002 tax return.

### What Is the EIC?

The EIC is a credit for certain workers. It reduces the tax you owe. It may give you a refund even if you do not owe any tax.

### Who Is Eligible To Get Advance EIC Payments?

You are eligible to get advance EIC payments if **all three** of the following apply.

1. You expect to have at least one qualifying child. If you do not expect to have a qualifying child, you may still be eligible for the EIC, but you **cannot** receive advance EIC payments. See **Who Is a Qualifying Child?** on page 2.

2. You expect that your 2002 earned income and AGI will each be less than \$29,201 (\$30,201 if you expect to file a joint return for 2002). Include your spouse's income if you plan to file a joint return. As used on this form, **earned income** does not include amounts inmates in penal institutions are paid for their work, amounts received as a pension or annuity from a nonqualified deferred compensation plan or a section 457 plan, or nontaxable earned income.

3. You expect to be able to claim the EIC for 2002. To find out if you may be able to claim the EIC, answer the questions on page 2.

**Workfare payments.** These are cash payments certain people receive from a state or local agency that administers public assistance programs funded under the Federal Temporary Assistance for Needy Families (TANF) program in return for certain work activities such as **(a)** work experience activities (including work associated with remodeling or repairing publicly assisted housing) if sufficient private sector employment is not available or **(b)** community service program activities.

### How To Get Advance EIC Payments

If you are eligible to get advance EIC payments, fill in the 2002 Form W-5 at the bottom of this page. Then, detach it and give it to your employer. If you get advance payments, you **must** file a 2002 Federal income tax return.

You may have only **one** Form W-5 in effect at one time. If you and your spouse are both employed, you should file separate Forms W-5.

(continued on page 2)

▼ Give the bottom part to your employer; keep the top part for your records. ▼

Detach here

Form <b>W-5</b>	<b>Earned Income Credit Advance Payment Certificate</b> ▶ Use the current year's certificate only. ▶ Give this certificate to your employer. ▶ This certificate expires on December 31, 2002.	OMB No. 1545-1342  <b>2002</b>
Department of the Treasury Internal Revenue Service	Print or type your full name	Your social security number
<p><b>Note:</b> If you get advance payments of the earned income credit for 2002, you <b>must</b> file a 2002 Federal income tax return. To get advance payments, you <b>must</b> have a qualifying child and your filing status must be any status <b>except</b> married filing a separate return.</p>		
<p>1 I expect to have a qualifying child and be able to claim the earned income credit for 2002, I do not have another Form W-5 in effect with any other current employer, and I choose to get advance EIC payments. . . <input type="checkbox"/> Yes <input type="checkbox"/> No</p> <p>2 Check the box that shows your expected filing status for 2002:  <input type="checkbox"/> Single, head of household, or qualifying widow(er) <input type="checkbox"/> Married filing jointly</p> <p>3 If you are married, does your spouse have a Form W-5 in effect for 2002 with any employer? . . . . . <input type="checkbox"/> Yes <input type="checkbox"/> No</p> <p><small>Under penalties of perjury, I declare that the information I have furnished above is, to the best of my knowledge, true, correct, and complete.</small></p>		
Signature ▶		Date ▶

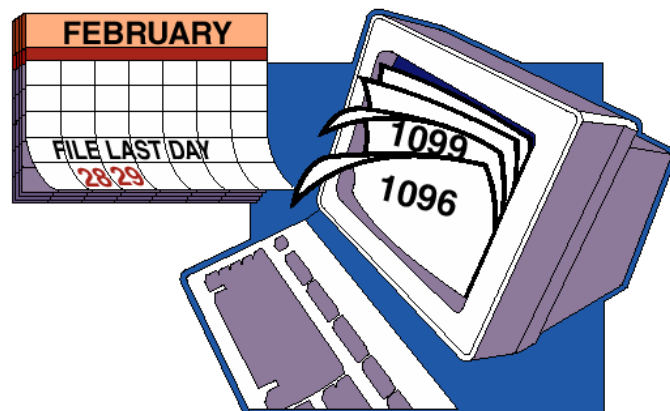
Cat. No. 10227P

## Form W-3 and Form 1096

Each year, you must file Form W-3, TRANSMITTAL OF WAGE AND TAX STATEMENTS, in order to transmit Copy A of Forms W-2 to the Social Security Administration by the last day of February after the calendar year for which the Forms W-2 are prepared. The Social Security Administration will process these forms and provide the IRS with the income tax data that it needs from those forms. The mailing address for the forms is on Form W-3.

**Note:** *The totals on the Form W-3 you file each year should equal the total of all Forms 941 filed for the year.*

Form 1096, Annual Summary and Transmittal of U.S. Information Returns, is used to transmit copy A of Forms 1099, 1098, 5498 and W-2G to the Internal Revenue Service. You must file Form 1096 with each type of return by February 28. If you file electronically, you may file by March 31.



In completing all transmittal documents (Forms W-3 and 1096) and information returns, you must use the same taxpayer identification number regardless of whether you file transmittals from more than one location. (See Exhibits 2.8 and 2.9.)

Use the same name on transmittals and information returns that you use on the income tax return or other returns you file under the same taxpayer identification number.

If information returns are prepared at different business locations, or if you are engaged in business with a “doing business as” (dba) name, there must be two name lines. The first name line contains the primary name (name shown on the income tax return). The second name line identifies the specific business location or is the “dba” name.

**Example 1**

A business has two different locations:  
Able Industries EIN: 10-0101010  
Shareholder Relations Dept.  
333 Main Street  
Mapleville, MO 33333

Able Industries EIN: 10-0101010  
Western Office  
222 Metropolitan Avenue  
Miliville, UT 22222

**Example 2**

The following taxpayers have “dba” names:

John Oak  
Maple City Auto Repair  
123 Main Street  
Maple City, NC 11111

Jane Apple  
Hometown Accounting Service  
25 Cherry Street  
Rosewood, OR 99999

**EXHIBIT 2.8 - BLANK FORM W-3**

DO NOT STAPLE OR FOLD

a Control number		33333		For Official Use Only ▶ OMB No. 1545-0008	
b Kind of Payer ▶	941 <input type="checkbox"/>	Military <input type="checkbox"/>	943 <input type="checkbox"/>	1 Wages, tips, other compensation	2 Federal income tax withheld
	CT-1 <input type="checkbox"/>	Hshid. emp. <input type="checkbox"/>	Medicare govt. emp. <input type="checkbox"/>	3 Social security wages	4 Social security tax withheld
	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	5 Medicare wages and tips	6 Medicare tax withheld
c Total number of Forms W-2	d Establishment number			7 Social security tips	8 Allocated tips
e Employer identification number				9 Advance EIC payments	10 Dependent care benefits
f Employer's name				11 Nonqualified plans	12 Deferred compensation
				13 For third-party sick pay use only	
g Employer's address and ZIP code				14 Income tax withheld by payer of third-party sick pay	
h Other EIN used this year					
15 State	Employer's state ID number			16 State wages, tips, etc.	17 State income tax
				18 Local wages, tips, etc.	19 Local income tax
Contact person				Telephone number	For Official Use Only
E-mail address				Fax number	

Under penalties of perjury, I declare that I have examined this return and accompanying documents, and, to the best of my knowledge and belief, they are true, correct, and complete.

Signature ▶ \_\_\_\_\_ Title ▶ \_\_\_\_\_ Date ▶ \_\_\_\_\_

Form **W-3** Transmittal of Wage and Tax Statements **2002** Department of the Treasury  
Internal Revenue Service

Send this entire page with the entire Copy A page of Form(s) W-2 to the Social Security Administration. Photocopies are not acceptable.

Do not send any payment (cash, checks, money orders, etc.) with Forms W-2 and W-3.

**An Item To Note**

Separate instructions. See the separate 2002 Instructions for Forms W-2 and W-3 for information on completing this form.

**Purpose of Form**

Use this form to transmit Copy A of Form(s) W-2, Wage and Tax Statement. Make a copy of Form W-3, and keep it with Copy D (For Employer) of Form(s) W-2 for your records. Use Form W-3 for the correct year. **File Form W-3 even if only one Form W-2 is being filed.** If you are filing Form(s) W-2 on magnetic media or electronically, **do not** file Form W-3.

**When To File**

File Form W-3 with Copy A of Form(s) W-2 by February 28, 2003.

**Where To File**

Send this entire page with the entire Copy A page of Form(s) W-2 to:

**Social Security Administration  
Data Operations Center  
Wilkes-Barre, PA 18769-0001**

**Note:** If you use "Certified Mail" to file, change the ZIP code to "18769-0002." If you use an IRS approved private delivery service, add "ATTN: W-2 Process, 1150 E. Mountain Dr." to the address and change the ZIP code to "18702-7997." See *Circular E, Employer's Tax Guide (Pub. 15)*, for a list of IRS approved private delivery services.

Do not send magnetic media to the address shown above.

For Privacy Act and Paperwork Reduction Act Notice, see the 2002 Instructions for Forms W-2 and W-3.

Cat. No. 10159Y

EXHIBIT 2.9 - BLANK FORM 1096

Do Not Staple **6969**

Form <b>1096</b> Department of the Treasury Internal Revenue Service	<b>Annual Summary and Transmittal of U.S. Information Returns</b>	OMB No. 1545-0108  <span style="font-size: 24pt; font-weight: bold;">2002</span>
FILER'S name  Street address (including room or suite number)  City, state, and ZIP code		
Name of person to contact  Telephone number ( )		<b>For Official Use Only</b> 
Fax number ( ) E-mail address		
1 Employer identification number	2 Social security number	3 Total number of forms
4 Federal income tax withheld \$		5 Total amount reported with this Form 1096 \$
Enter an "X" in only one box below to indicate the type of form being filed. If this is your final return, enter an "X" here. . . . <input type="checkbox"/>		
W-2G 32 <input type="checkbox"/>	1099-B 81 <input type="checkbox"/>	1099-E 84 <input type="checkbox"/>
1099-T 83 <input type="checkbox"/>	1099-A 80 <input type="checkbox"/>	1099-B 78 <input type="checkbox"/>
1099-C 85 <input type="checkbox"/>	1099-DIV 91 <input type="checkbox"/>	1099-G 86 <input type="checkbox"/>
1099-INT 92 <input type="checkbox"/>	1099-LTC 83 <input type="checkbox"/>	1099-MISC 85 <input type="checkbox"/>
1099-MSA 84 <input type="checkbox"/>	1099-CID 86 <input type="checkbox"/>	
1099-PATR 87 <input type="checkbox"/>	1099-Q 31 <input type="checkbox"/>	1099-R 86 <input type="checkbox"/>
1099-S 75 <input type="checkbox"/>	5498 28 <input type="checkbox"/>	5498-MSA 27 <input type="checkbox"/>

Please return this entire page to the Internal Revenue Service. Photocopies are not acceptable.

Under penalties of perjury, I declare that I have examined this return and accompanying documents, and, to the best of my knowledge and belief, they are true, correct, and complete.

Signature ▶	Title ▶	Date ▶
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**Instructions**

**Purpose of form.** Use this form to transmit paper Forms 1099, 1098, 5498, and W-2G to the Internal Revenue Service. Do not use Form 1096 to transmit magnetic media. See Form 4804, Transmittal of Information Returns Reported Magnetically.

**Who must file.** The name, address, and TIN of the filer on this form must be the same as those you enter in the upper left area of Form 1099, 1098, 5498, or W-2G. A filer includes a payer, a recipient of mortgage interest payments (including points) or student loan interest, an educational institution, a broker, a barter exchange, a creditor, a person reporting real estate transactions, a trustee or issuer of any individual retirement arrangement or an Archer MSA (including a Medicare+Choice MSA), and a lender who acquires an interest in secured property or who has reason to know that the property has been abandoned.

**Preaddressed Form 1096.** If you received a preaddressed Form 1096 from the IRS with Package 1099, use it to transmit paper Forms 1099, 1098, 5498, and W-2G to the Internal Revenue Service. If any of the imprinted information is incorrect, make corrections on the form.

**Note:** You will no longer receive an IRS-prepared label with your Package 1099.

If you are not using a preaddressed form, enter the filer's name, address (including room, suite, or other unit number), and TIN in the spaces provided on the form.

**When to file.** File Form 1096 with Forms 1099, 1098, or W-2G by February 28, 2003. File Form 1096 with Forms 5498 by June 2, 2003.

**Where To File**

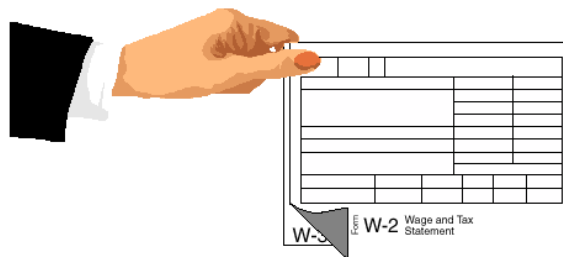
Send all information returns filed on paper with Form 1096 to the following:

If your principal business, office or agency, or legal residence in the case of an individual, is located in	Use the following Internal Revenue Service Center address
Alabama, Arizona, Florida, Georgia, Louisiana, Mississippi, New Mexico, North Carolina, Texas, Virginia	Austin, TX 73301
Arkansas, Connecticut, Delaware, Kentucky, Maine, Massachusetts, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Vermont, West Virginia	Cincinnati, OH 45999
Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Oklahoma, South Carolina, South Dakota, Tennessee, Wisconsin	Kansas City, MO 64999

For more information and the Privacy Act and Paperwork Reduction Act Notice, see the 2002 General Instructions for Forms 1099, 1098, 5498, and W-2G. Cat. No. 144000 Form 1096 (2002)

## Correcting Forms W-2 and W-3

If there is an error on Forms W-2 or W-3, correct by filing Form W-2c, CORRECTED WAGE AND TAX STATEMENT, and Form W-3c, TRANSMITTAL OF CORRECTED OF CORRECTED WAGE AND TAX STATEMENTS. (See instructions on the forms for detailed instructions)



## Filing on Magnetic Media or Electronically



Generally, the Social Security Administration will accept magnetic media or electronic records of Copy A for Forms W-2 or W-3 with prior approval. See the separate INSTRUCTIONS FOR FORM W-2 or W-3 for details about required magnetic media filing. If you file 250 or more Forms W-2 or 1099, you must file them on magnetic media or electronically. The 250 requirement applies separately for each type of information return and separately for each type of corrected return. When filed electronically, the due date is March 31 instead of February 28 to submit the forms.

The IRS encourages filers to transmit information returns electronically because it is generally more cost effective and easier than paper or magnetic media. To participate in the program, filers must submit a Form 4419, APPLICATION FOR FILING INFORMATION RETURNS MAGNETICALLY/ELECTRONICALLY, at least 30 days before the due date of the return(s) for current year processing.

### Information Reporting Call Site

The IRS operates a centralized call site to answer questions about reporting on Forms W-3, W-2, 1096 and 1099 and other information returns. If you have questions related to reporting on information returns, you may email them to [mccirp@irs.gov](mailto:mccirp@irs.gov) or call 1 (866) 455-7438 (toll-free), Monday through Friday, 8:30 A.M. to 4:30 P.M. (EST).

## Penalties

The following is a list of ten penalties that may be assessed for not complying with certain filing and payment requirements:

1. Failure to file.
2. Failure to pay.
3. Dishonored check.
4. Failure to timely file an information return with IRS or SSA.
5. Failure to timely furnish a copy of any information return to the payee.
6. Failure to file a partnership return.
7. Failure to make Federal Tax Deposits on time in an authorized government depository.
8. Failure to furnish specific information on an information return, such as including taxpayer identification numbers.
9. Failure to collect and/or pay over Trust Fund taxes (Trust Fund Recovery Penalty).
10. Failure to make deposits electronically if required to do so.

## Putting It All Together

### In this lesson you:

- briefly studied employment taxes;
- reviewed the Employer Identification Number (EIN);
- learned the definitions of “employee” and “independent contractor” for tax purposes;
- learned about Forms W-4, I-9 and information Forms 1099- MISC, W-9 and W-2;
- learned about Forms W-3 correct errors on Forms W-2 and W-3;
- read about transmitting Forms W-3, W-2, 1096 and 1099 on magnetic media or electronically and
- learned about 10 penalties that may be assessed for not complying with certain filing and payment requirements.



**In this lesson you were introduced to the following subjects:**

- federal income tax withheld from employees;
- social security and Medi-care taxes (withheld from employees and paid by employers) and federal unemployment taxes;
- successor employer and
- Earned Income Credit.

## Exercises

### Exercise 1

Bill Bean started a dry cleaning business and hired two employees. What form does he use to get an employer identification number?

\_\_\_\_\_

### Exercise 2

What form will your employee complete and give to you for you to determine how much income tax to withhold?

\_\_\_\_\_

### Exercise 3

(A) What are the social security tax and Medicare tax rates on an employee's salary in 2002?

(1) Social security tax rate \_\_\_\_\_%

(2) Medicare tax rate \_\_\_\_\_%

(B) What is the employer's share of each? \_\_\_\_\_

(C) What is the 2002 wage base limit for social security? \$\_\_\_\_\_

(D) What is the limit for Medicare? \_\_\_\_\_

### Exercise 4

(A) What form will you give to each employee to show wages paid, social security, Medicare and income taxes withheld? \_\_\_\_\_

(B) When is it due to the employee? \_\_\_\_\_

### Exercise 5

What form will you give an unincorporated independent contractor to whom you paid \$600 or more for services in the course of your trade or business? \_\_\_\_\_

**Exercise 6**

If you make payments to an unincorporated independent contractor who does not give you his or her identifying number, at what rate will you withhold taxes on the payments? \_\_\_\_\_%

**Exercise 7**

Mary Smith, your employee, wants advance payments of earned income credit added to her wages. What form should she complete and give to you? \_\_\_\_\_

**Exercise 8**

What forms will you use to correct a Form W-2 that is in error? \_\_\_\_\_ and \_\_\_\_\_

*(Answers found on page A-1.)*

## Lesson 3

# Part I: Form 941, Employer's Quarterly Federal Tax Return

### Introduction

If you are an employer who is required to withhold income or social security and Medicare taxes, you must file a return reporting the amounts withheld. Form 941, EMPLOYER'S QUARTERLY FEDERAL TAX RETURN, is used for this purpose. However, other forms are used in certain circumstances. (See Exhibit 3.1 on page 3-4.)



If you are a sole proprietor and file Form 941 for business employees, you may include household employees on the form. Also, if you operate a farm for profit and file Form 943, EMPLOYER'S ANNUAL TAX RETURN FOR AGRICULTURAL EMPLOYEES, for your agricultural employees, you may include farm household workers on that form.

**Form 945, ANNUAL RETURN OF WITHHELD FEDERAL INCOME TAX**, is used to report income tax withheld from non-payroll payments, such as pensions, IRAs, gambling winnings and backup withholding.

**Publication 15, EMPLOYER'S TAX GUIDE (Circular E)**, explains the rules and methods for withholding, paying, depositing and reporting federal income tax, social security and Medicare taxes and federal unemployment (FUTA) tax on wages, tips and fringe benefits. It also explains who is an employee, what are taxable wages and what are taxable tips.

**Publication 15-A, EMPLOYER'S SUPPLEMENTAL TAX GUIDE**, provides specialized information supplementing the basic employment tax information provided in Circular E, such as a more detailed discussion on the employment tax treatment of fringe benefits and information on how to report third-party sick pay.

**Publication 15-B, EMPLOYER'S TAX GUIDE TO FRINGE BENEFITS**, contains detailed information on fringe benefits and their exclusion and valuation rules.

**Objectives**

At the end of this lesson, you will be able to:

1. Determine Form 941 deposit requirements.
2. Prepare a Form 941.

**References**

Publication 15, EMPLOYER'S TAX GUIDE (Circular E)

Publication 15-A, EMPLOYER'S SUPPLEMENTAL TAX GUIDE

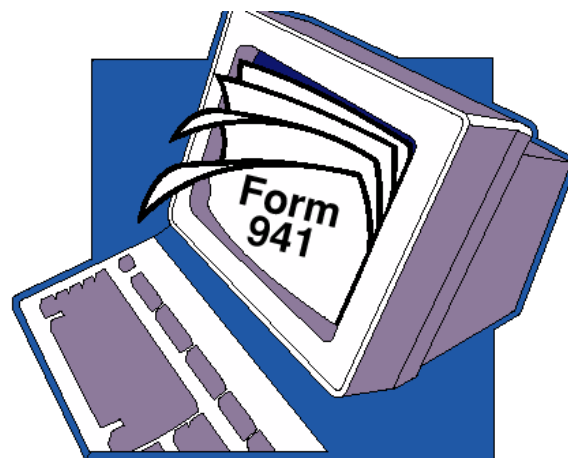
Publication 15-B, EMPLOYER'S TAX GUIDE TO FRINGE BENEFITS

**Due Dates for Filing Form 941****Form 941**

Form 941 is due the last day of the month after each quarter ends. The return filing dates are listed below:

<b>Due Dates for Filing Form 941</b>		
<b>Quarter</b>	<b>Ends</b>	<b>Due Date</b>
January, February, March	Mar. 31	Apr. 30*
April, May, June	June 30	July 31*
July, August, September	Sept. 30	Oct. 31*
October, November, December	Dec. 31	Jan. 31*

*\*If the due date for a return falls on a Saturday, Sunday or legal holiday, the due date is the next business day.*



If you paid the quarterly tax payments in full, you are allowed an additional 10 days to file the return. For example, your return for the quarter that ends on June 30 would be due on August 10 instead of July 31.

Do not file more than one Form 941 per quarter and do not report more than one calendar quarter on a return.

Seasonal employers are not required to file for quarters when they regularly have no tax liability because they have paid no wages. To alert the IRS that you will not have to file a return for one or more quarters during

the year, check the seasonal employer box above line 1 on Form 941 each time you file. The IRS will mail two Forms 941 to you once a year after March 1. The preprinted name and address information will not include the date the quarter ended. You must enter that date when you file the return.



If you are not a seasonal employer, but you receive a preaddressed Form 941 for a quarter in which you have no employees or may have temporarily stopped paying salaries, file a return anyway. This ensures that you will continue to receive Form 941 from the campus.

If you cease to do business or pay wages, you need to file a final return. The instructions for Form 941 give information on how to file if you sell, transfer or merge your business with another business.

Always use the preaddressed form mailed to you. If you do not receive a preaddressed form, print or type your name and address **exactly** as shown on the previous return unless the information has changed.

The date your quarter ends and your EIN must also be shown. If you have not yet received notification of your EIN, write “Applied for” and the date you applied in the space provided for the EIN.

**EXHIBIT 3.1 - BLANK FORM 941, EMPLOYER'S QUARTERLY FEDERAL TAX Return**

**Form 941**  
(Rev. January 2002)  
Department of the Treasury  
Internal Revenue Service (99)

**Employer's Quarterly Federal Tax Return**

▶ See separate instructions revised January 2002 for information on completing this return.

Please type or print.

OMB No. 1545-0029

T \_\_\_\_\_  
FF \_\_\_\_\_  
FD \_\_\_\_\_  
FP \_\_\_\_\_  
I \_\_\_\_\_  
T \_\_\_\_\_

Enter state code for state in which deposits were made **only** if different from state in address to the right ▶ [ ] (see page 2 of instructions).

Name (as distinguished from trade name) \_\_\_\_\_ Date quarter ended [ ]

Trade name, if any \_\_\_\_\_ Employer identification number \_\_\_\_\_

Address (number and street) \_\_\_\_\_ City, state, and ZIP code \_\_\_\_\_

If address is different from prior return, check here ▶

	1	1	1	1	1	1	1	1	1	2	3	3	3	3	3	3	3	4	4	4	5	5	5	
	6	7	8	8	8	8	8	8	8	8	9	9	9	9	9	9	9	9	10	10	10	10	10	10

IRS Use

If you do not have to file returns in the future, check here ▶  and enter date final wages paid ▶ [ ]

If you are a seasonal employer, see **Seasonal employers** on page 1 of the instructions and check here ▶

1 Number of employees in the pay period that includes March 12th . ▶ 1			
2 Total wages and tips, plus other compensation . . . . .	2		
3 Total income tax withheld from wages, tips, and sick pay . . . . .	3		
4 Adjustment of withheld income tax for preceding quarters of calendar year . . . . .	4		
5 Adjusted total of income tax withheld (line 3 as adjusted by line 4—see instructions) . . . . .	5		
6 Taxable social security wages . . . . .	6a		× 12.4% (.124) = 6b
Taxable social security tips . . . . .	6c		× 12.4% (.124) = 6d
7 Taxable Medicare wages and tips . . . . .	7a		× 2.9% (.029) = 7b
8 Total social security and Medicare taxes (add lines 6b, 6d, and 7b). Check here if wages are not subject to social security and/or Medicare tax . . . . . <input type="checkbox"/>	8		
9 Adjustment of social security and Medicare taxes (see instructions for required explanation) Sick Pay \$ _____ ± Fractions of Cents \$ _____ ± Other \$ _____ =	9		
10 Adjusted total of social security and Medicare taxes (line 8 as adjusted by line 9—see instructions) . . . . .	10		
11 Total taxes (add lines 5 and 10) . . . . .	11		
12 Advance earned income credit (EIC) payments made to employees . . . . .	12		
13 Net taxes (subtract line 12 from line 11). If \$2,500 or more, this must equal line 17, column (d) below (or line D of Schedule B (Form 941))	13		
14 Total deposits for quarter, including overpayment applied from a prior quarter . . . . .	14		
15 Balance due (subtract line 14 from line 13). See instructions . . . . .	15		
16 Overpayment. If line 14 is more than line 13, enter excess here ▶ \$ _____ and check if to be: <input type="checkbox"/> Applied to next return or <input type="checkbox"/> Refunded.			

- All filers: If line 13 is less than \$2,500, you need not complete line 17 or Schedule B (Form 941).
- Semiweekly schedule depositors: Complete Schedule B (Form 941) and check here . . . . . ▶
- Monthly schedule depositors: Complete line 17, columns (a) through (d), and check here. . . . . ▶

**17 Monthly Summary of Federal Tax Liability.** Do not complete if you were a semiweekly schedule depositor.

(a) First month liability	(b) Second month liability	(c) Third month liability	(d) Total liability for quarter

Third Party Designee: Do you want to allow another person to discuss this return with the IRS (see separate instructions)?  Yes. Complete the following.  No

Designee's name ▶ \_\_\_\_\_ Phone no. ▶ ( ) \_\_\_\_\_ Personal identification number (PIN) ▶ [ ] [ ] [ ] [ ] [ ] [ ]

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

Signature = \_\_\_\_\_ Print Your Name and Title = \_\_\_\_\_ Date = \_\_\_\_\_

For Privacy Act and Paperwork Reduction Act Notice, see back of Payment Voucher. Cat. No. 170012 Form 941 (Rev. 1-2002)

3-4

## Form 941

Complete the state code boxes if you made your deposits in a state other than that shown in your address on Form 941. Enter the state code for the state where you made deposits in the box provided in the upper left corner of the form. Enter code “MU” in the box if you deposit in more than one state. **If you deposit in the same state as shown in your address, do not make an entry.** If you deposited electronically (discussed on page 3-10) do not make an entry here.

Complete lines 1 through 17, if applicable. Specific Form 941 line entries are discussed below. More complete information on these line entries is contained in the instructions for Form 941.

### **Line 1.**

Make an entry for the pay period including March 12, on the 1<sup>st</sup> quarter (January–March) return only.

### **Line 2.**

Enter the total of: all wages paid, tips reported, taxable fringe benefits provided and other compensation paid to your employees, even if you do not have to withhold income tax or social security tax on it. Do not include contributions to employee plans that are excluded from the employee’s wages (e.g., section 401(k) and 125 plans).

### **Line 3.**

Enter the income tax you withheld on wages, tips, taxable fringe benefits and certain other payments.

### **Line 6a.**

Taxable social security wages. Enter the total wages subject to social security taxes that you paid your employees during the quarter. Also include any sick pay and taxable fringe benefits subject to social security taxes. Stop reporting when an employee’s wages (including tips) reach the wage base (\$84,900 in 2002). Multiply by the applicable percentage printed on the line.

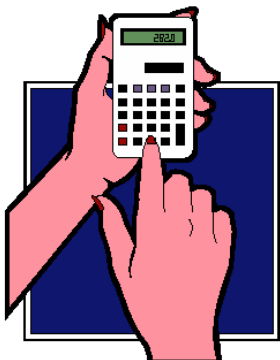
### **Line 6c.**

Taxable social security tips. Enter all tips your employees reported during the quarter, until tips and wages for an employee reach the wage base amount (\$84,900 in 2002). Do this even if you were not able to withhold the employee social security tax. See the Form 941 instructions for details on how to make an adjustment for uncollected social security tax on tips.

### **Line 7a.**

Taxable Medicare wages and tips. Report all wages and tips, including any sick pay and taxable fringe benefits subject to Medicare tax. There is no limit on the amount of wages subject to





Medicare.

**Line 8.**

Total social security and Medicare taxes. Check the box if none of the wages are subject to social security or Medicare taxes.

**Line 9.**

Adjustment of social security and Medicare taxes. A fractions-of-cents adjustment is the small difference that may occur between net taxes (line 13) and total deposits (line 14), because of rounding to the nearest cent each time you computed payroll. This rounding occurs when you figure the amount of social security and Medicare taxes to be withheld from each employee's wages.

To determine if you have a fractions-of-cents adjustment, multiply the total wages and tips for the quarter by the applicable percentage and compare these amounts with the total social security and Medicare taxes actually withheld from your payroll records. The difference, positive or negative, is your fractions-of-cents adjustment.

See Publication 15 for instructions on other adjustments.

**Line 12.**

Enter any advance EIC payments made to employees.

**Line 13.**

Net taxes. Make sure the line equals line 17, column (d) below (or line D of Schedule B (Form 941)). (See Exhibit 3.2 on page 3-7.)

***Note: If line 13 is \$2,500 or more, check the appropriate box below Line 16 indicating your depositor status.***

**EXHIBIT 3.2 - FORM 941, SCHEDULE B, EMPLOYER'S RECORD Federal TAX LIABILITY**

<p><b>SCHEDULE B (FORM 941)</b> (Rev. January 2002) Department of the Treasury Internal Revenue Service</p>	<p><b>Employer's Record of Federal Tax Liability</b></p> <p>▶ See Circular E for more information about employment tax returns.</p> <p>▶ Attach to Form 941 or 941-SS.</p>	<p>OMB No. 1545-0029</p>				
<p>5151</p>						
<p>Name as shown on Form 941 (or Form 941-SS)</p>		<p>Employer identification number</p>				
		<p>Date quarter ended</p>				
<p>You must complete this schedule if you are required to deposit on a semiweekly schedule, or if your tax liability on any day is \$100,000 or more. Show tax liability here, <b>not</b> deposits. (The IRS gets deposit data from FTD coupons or EFTPS.)</p>						
<p><b>A. Daily Tax Liability—First Month of Quarter</b></p>						
1	8	15	22	29		
2	9	16	23	30		
3	10	17	24	31		
4	11	18	25			
5	12	19	26			
6	13	20	27			
7	14	21	28			
<p><b>A</b> Total tax liability for first month of quarter . . . . . ▶</p>					<b>A</b>	
<p><b>B. Daily Tax Liability—Second Month of Quarter</b></p>						
1	8	15	22	29		
2	9	16	23	30		
3	10	17	24	31		
4	11	18	25			
5	12	19	26			
6	13	20	27			
7	14	21	28			
<p><b>B</b> Total tax liability for second month of quarter . . . . . ▶</p>					<b>B</b>	
<p><b>C. Daily Tax Liability—Third Month of Quarter</b></p>						
1	8	15	22	29		
2	9	16	23	30		
3	10	17	24	31		
4	11	18	25			
5	12	19	26			
6	13	20	27			
7	14	21	28			
<p><b>C</b> Total tax liability for third month of quarter . . . . . ▶</p>					<b>C</b>	
<p><b>D</b> Total for quarter (add lines A, B, and C). This should equal line 13 of Form 941 (or line 10 of Form 941-SS) ▶</p>					<b>D</b>	
<p>For Paperwork Reduction Act Notice, see page 2.</p>			<p>Cat. No. 11967Q</p>	<p>Schedule B (Form 941) (Rev. 1-2002)</p>		

## Monthly Summary of Federal Tax Liability

Report on **line 17** your employment tax liability for each month based on the date the corresponding wages were paid, not when the payroll period ends. If your total taxes for the quarter are \$2,500 or more, you must instead complete a separate Schedule B, EMPLOYER'S RECORD OF FEDERAL TAX LIABILITY, page 3-7 (Exhibit 3.2).



Tax liability is income tax withheld plus both the employee and employer shares of social security and Medicare taxes, minus any advance earned income credit (EIC) payments.

## Filing by Other Methods



You may be able to file Form 941 by phone if you meet certain criteria. On-line filing through a personal computer is also an option.

Reporting Agents who file Forms 941 for groups of taxpayers can file them electronically or on tape. See Lesson 5 and Publication 15-A for details.

Beginning in January 2003, tax professionals can file 941 returns electronically. The tax professional must be an authorized e-file provider. See Publication 3112 for more information.

Now that you have covered the background information, you will learn how deposits are made, how information is entered on the form and how the tax due is figured.

## Depositing Requirements

In general, you must deposit income tax withheld and both the employer and employee social security and Medicare taxes (minus any advance EIC payments) using the Electronic Federal Payment System (EFTPS) or by mailing or delivering a check, money order or cash to an authorized financial institution or Federal Reserve bank with Form 8109, FEDERAL TAX DEPOSIT COUPON. Some taxpayers are required to deposit using EFTPS.

## Payment With Return

You may make a payment with Form 941 instead of depositing it if your net tax liability (reduced by any advance earned income credit) during the quarter (line 13 of Form 941) is less than \$2,500. (Exhibit 3.3) See Publication 15 for exceptions.

**EXHIBIT 3.3 - FORM 941, PAYMENT VOUCHER**

▼ Detach Here and Mail With Your Payment ▼		Form <b>941-V</b> (2002)	
<b>Form 941-V</b> Department of the Treasury Internal Revenue Service (99)		<b>Payment Voucher</b>	
		OMB No. 1545-0029	
▶ Do not staple or attach this voucher to your payment.		<b>2002</b>	
<b>1</b> Enter your employer identification number  ..... .....	<b>2</b> Enter the amount of the payment	Dollars	Cents
<b>3</b> Tax period  <input type="checkbox"/> 1st Quarter <input type="checkbox"/> 3rd Quarter <input type="checkbox"/> 2nd Quarter <input type="checkbox"/> 4th Quarter	<b>4</b> Enter your business name (individual name if sole proprietor)  Enter your address  Enter your city, state, and ZIP code		

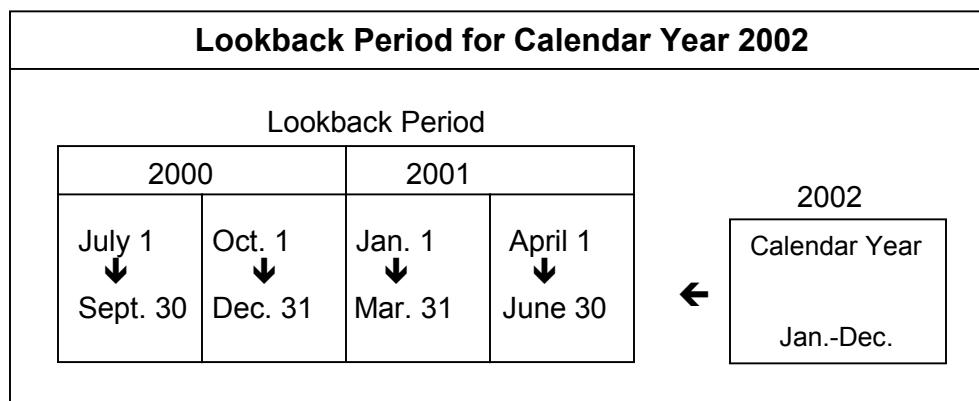
## When to Deposit

There are two deposit schedules – **monthly or semiweekly** – for determining when you deposit social security, Medicare and withheld income taxes. These schedules tell you when a deposit is due after a tax liability arises (e.g., when you have a payday).

## Lookback Period

Your deposit schedule for a calendar year is determined from the total taxes (not reduced by any advance EIC payments) reported on your Forms 941 (line 11) in a four-quarter lookback period. The lookback period for Form 941 filers begins July 1 and ends June 30. (See Exhibit 3.4.) If you reported \$50,000 or less of taxes for the lookback period, you are a monthly schedule depositor; if you reported more than \$50,000 you are a semiweekly schedule depositor.

**EXHIBIT 3.4 – LOOKBACK PERIOD FOR CALENDAR YEAR 2002**



**Monthly Deposit Schedule**

Under the monthly deposit schedule, deposit Form 941 taxes on payments made during a month by the 15<sup>th</sup> day of the following month.

Note to new employers: During the first calendar year of your business, your tax liability for each quarter, in the lookback period, is considered to be zero. Therefore, you are a monthly schedule depositor for the first calendar year of your business unless the \$100,000 Next-Day Deposit rule (discussed on page 3-11) applies.

**Semiweekly Deposit Schedule**

You are a semiweekly schedule depositor for a calendar year if the total taxes on Form 941 (line 11) during your lookback period were more than \$50,000. If the payday falls on Wednesday, Thursday and /or Friday, you must deposit the Form 941 taxes no later than the following Wednesday. (See Exhibit 3.5 below.) If the payday falls on Saturday, Sunday, Monday and/or Tuesday, deposit by Friday.

**EXHIBIT 3.5 – SEMIWEEKLY DEPOSIT SCHEDULE**

<b>Semiweekly Deposit Schedule</b>	
<b>IF the day falls on a...</b>	<b>THEN deposit taxes by the following...</b>
Wednesday, Thursday and/or Friday	Wednesday
Saturday, Sunday, Monday and/or Tuesday	Friday

**Application of Monthly and Semiweekly Schedule**

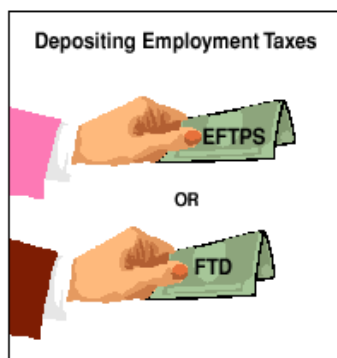
The terms “monthly schedule depositor” and “semiweekly schedule depositor” do not refer to how often your business pays its employees or even how often you are required to make deposits. These terms identify a set of deposit rules you must follow when employment tax liability occurs and are based on the date wages are paid.

## **\$100,000 Next-Day Deposit Rule**

If you accumulate a tax liability (reduced by any advance EIC payments) of \$100,000 or more on any day during a deposit period, you must deposit the tax by the next banking day, regardless of whether you are a monthly or semiweekly schedule depositor. The term deposit period refers to the period during which tax liabilities are accumulated for each required deposit due date. For monthly schedule depositors, the deposit period is a calendar month. If you are a monthly depositor and become subject to the rule, you become a semiweekly depositor for the remainder of the year and all of the following year.

The two methods of depositing employment taxes are by EFTPS and by using Federal Tax Deposit (FTD) coupons (Form 8109).

You are required to make electronic deposits using EFTPS of **all** your tax liabilities in 2002 if your total deposits of **all** federal depository taxes were more than \$200,000 in 2000 or if you were required to use EFTPS in 2001. For more details, see Publication 15 and Lesson 5.



If you are not required to use EFTPS, you can make your required deposits at an authorized financial institution or Federal Reserve bank (FRB) using FTD coupons. (See Exhibit 3.6 on page 3-12). The IRS will issue you a book of coupons 5 to 6 weeks after you receive your EIN.

**Note: Even if you are not required to make electronic tax deposits, you may voluntarily participate in EFTPS. To enroll, call 1-800-945-8400 or 1-800-555-4477.**

An employer may be penalized for using the wrong deposit method. Always ensure your deposits are timely because late deposits are subject to penalties. Check with your local depository or FRB for information concerning their cutoff time (exact hour they start dating deposits as received on their next banking day).

**EXHIBIT 3.6 – BLANK FORM 8109, FEDERAL TAX DEPOSIT COUPON**

**Example**

Smith Enterprises, Inc.  
 EIN: 10-1614316  
 1512 Poplar St.  
 Inn, MI 48200

Period Ending	Number of Employees	Gross Wages	*FICA Withheld	*Employer's FICA	Income Tax Withheld
1/31/02	4	\$4,800	\$367.20	\$367.20	\$400.00
2/28/02	4	4,750	363.38	363.38	406.00
3/31/02	3	4,200	321.30	321.30	340.00
Quarterly Totals		\$13,750	\$1,051.88	\$1,051.88	\$1,146.00
*Social security and Medicare taxes referred to as FICA.					

Smith Enterprises, Inc., as a monthly depositor, must deposit each month's taxes by the 15th of the following month (\$1,134.40 by February 15; \$1,132.76 by March 15 and \$982.60 by April 15). If the **total** taxes for all three months of the quarter had been less than \$2,500, then they could have been deposited or paid with the Form 941 to be filed by April 30, 2002.

(Exhibit 3.7 on page 3-12 uses this information to complete Form 941.)

EXHIBIT 3.7 – FORM 941, EMPLOYER’S QUARTERLY FEDERAL TAX RETURN

**Form 941**  
(Rev. January 2002)  
Department of the Treasury  
Internal Revenue Service (99)

**Employer’s Quarterly Federal Tax Return**

▶ See separate instructions revised January 2002 for information on completing this return.

Please type or print.

OMB No. 1545-0029

T

FF

FD

FP

I

T

Enter state code for state in which deposits were made **only** if different from state in address to the right ▶  (see page 2 of instructions).

Name (as distinguished from trade name) **Smith Enterprises, Inc.**

Trade name, if any **D**

Address (number and street) **1512 Poplar St.**

Date quarter ended **3-31-2002**

Employer identification number **10-1614316**

City, state, and ZIP code **Inn, MI 48200**

If address is different from prior return, check here ▶

1	1	1	1	1	1	1	1	1	1	2	3	3	3	3	3	3	3	4	4	4	5	5	5	
6	7	8	8	8	8	8	8	8	8	9	9	9	9	9	9	9	9	9	10	10	10	10	10	10

If you do not have to file returns in the future, check here ▶  and enter date final wages paid ▶

If you are a seasonal employer, see **Seasonal employers** on page 1 of the instructions and check here ▶

1 Number of employees in the pay period that includes March 12th . . . ▶	1	3	
2 Total wages and tips, plus other compensation . . . . .	2	13,750	00
3 Total income tax withheld from wages, tips, and sick pay . . . . .	3	1,146	00
4 Adjustment of withheld income tax for preceding quarters of calendar year . . . . .	4		
5 Adjusted total of income tax withheld (line 3 as adjusted by line 4—see instructions) . . . . .	5	1,146	00
6 Taxable social security wages . . . . .	6a	13,750	00
		× 12.4% (.124) =	
6c Taxable social security tips . . . . .	6c		
		× 12.4% (.124) =	
7 Taxable Medicare wages and tips . . . . .	7a	13,750	00
		× 2.9% (.029) =	
7b		398	75
8 Total social security and Medicare taxes (add lines 6b, 6d, and 7b). Check here if wages are not subject to social security and/or Medicare tax . . . . .	8	2,103	75
9 Adjustment of social security and Medicare taxes (see instructions for required explanation) Sick Pay \$ ± Fractions of Cents \$ <b>*.01</b> ± Other \$ =	9		01
10 Adjusted total of social security and Medicare taxes (line 8 as adjusted by line 9—see instructions) . . . . .	10	2,103	76
11 Total taxes (add lines 5 and 10) . . . . .	11	3,249	76
12 Advance earned income credit (EIC) payments made to employees . . . . .	12		
13 Net taxes (subtract line 12 from line 11). If \$2,500 or more, this must equal line 17, column (d) below (or line D of Schedule B (Form 941)) . . . . .	13	3,249	76
14 Total deposits for quarter, including overpayment applied from a prior quarter . . . . .	14	3,249	76
15 Balance due (subtract line 14 from line 13). See instructions . . . . .	15		
16 Overpayment. If line 14 is more than line 13, enter excess here ▶ \$ and check if to be: <input type="checkbox"/> Applied to next return or <input type="checkbox"/> Refunded.			

All filers: If line 13 is less than \$2,500, you need not complete line 17 or Schedule B (Form 941).  
 Semiweekly schedule depositors: Complete Schedule B (Form 941) and check here . . . . .  
 Monthly schedule depositors: Complete line 17, columns (a) through (d), and check here. . . . .

17 Monthly Summary of Federal Tax Liability. Do not complete if you were a semiweekly schedule depositor.			
(a) First month liability	(b) Second month liability	(c) Third month liability	(d) Total liability for quarter
1,344.40	1,132.70	982.00	3,249.76

Do you want to allow another person to discuss this return with the IRS (see separate instructions)?  Yes. Complete the following.  No

Third Party Designee name ▶ **y** Phone no. ▶ ( ) Personal identification number (PIN) ▶

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

Signature ▶ **Helen Smith** Print Your Name and Title ▶ **Helen Smith, Pres.** Date ▶

For Privacy Act and Paperwork Reduction Act Notice, see back of Payment Voucher. Cat. No. 17001Z Form 941 (Rev. 1-2002)

3-13



## Deposit Penalties

Deposits not made in a timely manner may be subject to penalties. For amounts not properly or timely deposited, the penalty rates are:

- **2%** - Deposits made 1 to 5 days late.
- **5%** - Deposits made 6 to 15 days late.
- **10%** - Deposits made 16 or more days late.
- **10%** - Deposits made at an unauthorized financial institution, paid directly to the IRS or paid with your tax return. See Publication 15 for exceptions.
- **10%** - Amounts that are subject to electronic deposit requirements but not deposited using EFTPS.
- **15%** - Amounts still unpaid more than 10 days after the date of the first notice the IRS sent asking for the tax due or the day on which you receive notice and demand for immediate payment, whichever is earlier.

## Correcting Form 941

Errors made in figuring taxes in an earlier quarter can be corrected on a current Form 941 by making an adjustment to the current quarter's taxes. Circular E describes in detail how to correct errors to income tax withholding, social security and Medicare taxes.

*Note: You may not adjust or claim a refund or credit for any overpayment of income tax that you withheld or deducted from an employee in a prior year. But see Circular E for information on administrative error adjustments.*

## Summary

In this lesson, you studied:

- Form 941 and its due dates,
- deposit requirements,
- the method of depositing taxes due and
- some of the sections and lines of Form 941.



Remember: Form 941 is a quarterly return, but deposits may be required on a monthly or semiweekly schedule.

## Exercises

### Exercise 1

Green for Ever, Inc.  
 EIN: 10-1234567  
 925 Fern Ave.  
 Augusta, GA 32599

Pay Date	Number of Employees	Gross Wages	*Social Security Tax Withheld	*Medicare Tax Withheld	Income Tax Withheld
4/5/02	2	\$2,050	\$127.10	\$29.73	\$163.00
4/19/02	3	3,805	235.91	55.17	285.00
5/3/02	4	5,545	343.79	80.40	4356.00
5/17/02	4	5,975	370.45	86.64	373.00
5/31/02	4	5,050	313.10	73.23	328.00
6/14/02	3	4,405	273.11	63.87	467.00
Totals		26,830	1,663.46	389.04	1,972.00
*Employer must match these amounts.					

First, figure the amount and date of deposits (the company is a monthly depositor). Then complete a Form 941 (Exhibit 3.8) using the information provided.

Deposit dates and amounts are:

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

Total deposits \$ \_\_\_\_\_

*(Answers are found on pages A-2 and A-3.)*

**EXHIBIT 3.8 - BLANK FORM 941, EMPLOYER'S QUARTERLY FEDERAL TAX RETURN FOR EXERCISE 1**

Form **941**  
 (Rev. January 2002)  
 Department of the Treasury  
 Internal Revenue Service (99)

**Employer's Quarterly Federal Tax Return**  
 ▶ See separate instructions revised January 2002 for information on completing this return.  
 Please type or print.

Enter state code for state in which deposits were made **only** if different from state in address to the right ▶ (see page 2 of instructions).

Name (as distinguished from trade name) \_\_\_\_\_ Date quarter ended \_\_\_\_\_

Trade name, if any \_\_\_\_\_ Employer identification number \_\_\_\_\_

Address (number and street) \_\_\_\_\_ City, state, and ZIP code \_\_\_\_\_

OMB No. 1545-0029

T \_\_\_\_\_  
 FF \_\_\_\_\_  
 FD \_\_\_\_\_  
 FP \_\_\_\_\_  
 I \_\_\_\_\_  
 T \_\_\_\_\_

If address is different from prior return, check here ▶

1	1	1	1	1	1	1	1	1	1	2	3	3	3	3	3	3	3	4	4	4	5	5	5
6	7	8	8	8	8	8	8	8	8	8	9	9	9	9	9	9	9	10	10	10	10	10	10

If you do not have to file returns in the future, check here ▶  and enter date final wages paid ▶ \_\_\_\_\_  
 If you are a seasonal employer, see **Seasonal employers** on page 1 of the instructions and check here ▶

1 Number of employees in the pay period that includes March 12th . . . ▶ <b>1</b>			
2 Total wages and tips, plus other compensation . . . . .	2		
3 Total income tax withheld from wages, tips, and sick pay . . . . .	3		
4 Adjustment of withheld income tax for preceding quarters of calendar year . . . . .	4		
5 Adjusted total of income tax withheld (line 3 as adjusted by line 4—see instructions) . . . . .	5		
6 Taxable social security wages . . . . .	6a		× 12.4% (.124) = 6b
Taxable social security tips . . . . .	6c		× 12.4% (.124) = 6d
7 Taxable Medicare wages and tips . . . . .	7a		× 2.9% (.029) = 7b
8 Total social security and Medicare taxes (add lines 6b, 6d, and 7b). Check here if wages are not subject to social security and/or Medicare tax . . . . . ▶ <input type="checkbox"/>	8		
9 Adjustment of social security and Medicare taxes (see instructions for required explanation) Sick Pay \$ _____ ± Fractions of Cents \$ _____ ± Other \$ _____ =	9		
10 Adjusted total of social security and Medicare taxes (line 8 as adjusted by line 9—see instructions) . . . . .	10		
11 <b>Total taxes</b> (add lines 5 and 10) . . . . .	11		
12 Advance earned income credit (EIC) payments made to employees . . . . .	12		
13 Net taxes (subtract line 12 from line 11). <b>If \$2,500 or more, this must equal line 17, column (d) below (or line D of Schedule B (Form 941))</b> . . . . .	13		
14 Total deposits for quarter, including overpayment applied from a prior quarter . . . . .	14		
15 <b>Balance due</b> (subtract line 14 from line 13). See instructions . . . . .	15		
16 <b>Overpayment.</b> If line 14 is more than line 13, enter excess here ▶ \$ _____ and check if to be: <input type="checkbox"/> Applied to next return <b>or</b> <input type="checkbox"/> Refunded.			

- **All filers:** If line 13 is less than \$2,500, you need not complete line 17 or Schedule B (Form 941).
- **Semiweekly schedule depositors:** Complete Schedule B (Form 941) and check here . . . . . ▶
- **Monthly schedule depositors:** Complete line 17, columns (a) through (d), and check here. . . . . ▶

17 Monthly Summary of Federal Tax Liability. Do not complete if you were a semiweekly schedule depositor.			
(a) First month liability	(b) Second month liability	(c) Third month liability	(d) Total liability for quarter

Third Party Designee: Do you want to allow another person to discuss this return with the IRS (see separate instructions)?  Yes. Complete the following.  No

Designee's name ▶ \_\_\_\_\_ Phone no. ▶ ( ) \_\_\_\_\_ Personal identification number (PIN) ▶ \_\_\_\_\_

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

Signature ▶ \_\_\_\_\_ Print Your Name and Title ▶ \_\_\_\_\_ Date ▶ \_\_\_\_\_

**Exercise 2**

In May 2002, you decide to employ your 16 year-old son\* to assist you in your yard service business, Glenn's Landscaping (a sole proprietorship). You are advised to have him complete a Form W-4, which he does, showing no (0) withholding allowances and single filing status. It is agreed that he will earn \$5.00 per hour and be paid every two weeks. He had worked 36 hours when it came time to make out his first paycheck. Using Publication 15 as a reference, answer the following:

How much should you withhold from his check?

\*Social Security Tax                   \$ \_\_\_\_\_

Medicare Tax                           \$ \_\_\_\_\_

Federal Income Tax                   \$ \_\_\_\_\_

*\*See page 28 (Family Employees) of Publication 15.*

*(Answers are found on page A-2.)*

**Exercise 3**

Paul's Auto Shop, Inc.  
EIN 10-9876543  
425 Auto Strip Dr.  
Cando, LA 88877

Pay Date	Number of Employees	Gross Wages	*Social Security Tax Withheld	*Medicare Tax Withheld	Income Tax Withheld Before AEIC	AEIC Payments
10/4/02	20	\$30.025	\$1,861.55	\$435.36	\$5,980.00	\$45.00
10/18/02	20	29,826	1,849.12	432.48	5,726.00	36.00
11/1/02	18	27.500	1,705.00	398.75	5,335.00	28.00
11/15/02	18	28.845	1,788.39	418.25	5,576.00	14.00
11/29/02	20	26.214	1,625.27	380.10	5,433.00	20.00
12/13/02	20	30.025	1,861.55	435.36	5,980.00	45.00
12/27/02	20	30.025	1,861.55	435.36	5,980.00	45.00
Totals		\$206.460	\$12,800.43	\$2,993.66	\$40,165.00	\$236.00
12/27/02 (Bonus)	20	4.000	248.00	58.00	155.00	3.00
*Employer must match these amounts.						

First, figure the amount and date of deposits (the corporation is a semiweekly depositor). Then complete a Form 941 and a Schedule B (Exhibit 3.9), using the information provided.

Deposit dates and amounts are:

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Total deposits \$ \_\_\_\_\_

*(Answers are found on pages A-2 and A-4.)*

**EXHIBIT 3.9 - BLANK FORM 941, EMPLOYER'S QUARTERLY FEDERAL TAX RETURN FOR EXERCISE 3**

Form **941**  
(Rev. January 2002)  
Department of the Treasury  
Internal Revenue Service (99)

**Employer's Quarterly Federal Tax Return**

▶ See separate instructions revised January 2002 for information on completing this return.

Please type or print.

Enter state code for state in which deposits were made **only** if different from state in address to the right ▶ (see page 2 of instructions).

Name (as distinguished from trade name) \_\_\_\_\_ Date quarter ended \_\_\_\_\_

Trade name, if any \_\_\_\_\_ Employer identification number \_\_\_\_\_

Address (number and street) \_\_\_\_\_ City, state, and ZIP code \_\_\_\_\_

OMB No. 1545-0029

T
FF
FD
FP
I
T

If address is different from prior return, check here ▶

IRS Use

1	1	1	1	1	1	1	1	1	1	2	3	3	3	3	3	3	3	3	4	4	4	5	5	5
6	7	8	8	8	8	8	8	8	8	8	9	9	9	9	9	9	9	9	10	10	10	10	10	10

If you do not have to file returns in the future, check here ▶  and enter date final wages paid ▶ \_\_\_\_\_  
If you are a seasonal employer, see **Seasonal employers** on page 1 of the instructions and check here ▶ \_\_\_\_\_

<b>1</b> Number of employees in the pay period that includes March 12th ▶ <b>1</b>		
<b>2</b> Total wages and tips, plus other compensation . . . . .	<b>2</b>	
<b>3</b> Total income tax withheld from wages, tips, and sick pay . . . . .	<b>3</b>	
<b>4</b> Adjustment of withheld income tax for preceding quarters of calendar year . . . . .	<b>4</b>	
<b>5</b> Adjusted total of income tax withheld (line 3 as adjusted by line 4—see instructions) . . . . .	<b>5</b>	
<b>6</b> Taxable social security wages . . . . .	<b>6a</b>	× 12.4% (.124) = <b>6b</b>
<b>6c</b> Taxable social security tips . . . . .	<b>6c</b>	× 12.4% (.124) = <b>6d</b>
<b>7</b> Taxable Medicare wages and tips . . . . .	<b>7a</b>	× 2.9% (.029) = <b>7b</b>
<b>8</b> Total social security and Medicare taxes (add lines 6b, 6d, and 7b). Check here if wages are not subject to social security and/or Medicare tax . . . . . ▶ <input type="checkbox"/>	<b>8</b>	
<b>9</b> Adjustment of social security and Medicare taxes (see instructions for required explanation) Sick Pay \$ _____ ± Fractions of Cents \$ _____ ± Other \$ _____ =	<b>9</b>	
<b>10</b> Adjusted total of social security and Medicare taxes (line 8 as adjusted by line 9—see instructions) . . . . .	<b>10</b>	
<b>11</b> Total taxes (add lines 5 and 10) . . . . .	<b>11</b>	
<b>12</b> Advance earned income credit (EIC) payments made to employees . . . . .	<b>12</b>	
<b>13</b> Net taxes (subtract line 12 from line 11). If \$2,500 or more, this must equal line 17, column (d) below (or line D of Schedule B (Form 941)) . . . . .	<b>13</b>	
<b>14</b> Total deposits for quarter, including overpayment applied from a prior quarter . . . . .	<b>14</b>	
<b>15</b> Balance due (subtract line 14 from line 13). See instructions . . . . .	<b>15</b>	
<b>16</b> Overpayment. If line 14 is more than line 13, enter excess here ▶ \$ _____ and check if to be: <input type="checkbox"/> Applied to next return or <input type="checkbox"/> Refunded.		

- All filers: If line 13 is less than \$2,500, you need not complete line 17 or Schedule B (Form 941).
- Semiweekly schedule depositors: Complete Schedule B (Form 941) and check here . . . . . ▶
- Monthly schedule depositors: Complete line 17, columns (a) through (d), and check here. . . . . ▶

<b>17 Monthly Summary of Federal Tax Liability.</b> Do not complete if you were a semiweekly schedule depositor.			
(a) First month liability	(b) Second month liability	(c) Third month liability	(d) Total liability for quarter

Third Party Designee Do you want to allow another person to discuss this return with the IRS (see separate instructions)?  Yes. Complete the following.  No

Designee's name ▶ \_\_\_\_\_ Phone no. ▶ ( ) \_\_\_\_\_ Personal identification number (PIN) ▶ \_\_\_\_\_

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

Signature ▶ \_\_\_\_\_ Print Your Name and Title ▶ \_\_\_\_\_ Date ▶ \_\_\_\_\_

**EXHIBIT 3.9 - BLANK SCHEDULE B, FORM 941, EMPLOYER’S RECORD OF FEDERAL TAX LIABILITY FOR EXERCISE 3**

<b>SCHEDULE B (FORM 941)</b> <small>(Rev. January 2002) Department of the Treasury Internal Revenue Service</small>		<b>Employer's Record of Federal Tax Liability</b> ▶ See Circular E for more information about employment tax returns. 5151 ▶ Attach to Form 941 or 941-SS.			OMB No. 1545-0029	
Name as shown on Form 941 (or Form 941-SS)				Employer identification number		Date quarter ended
You must complete this schedule if you are required to deposit on a semiweekly schedule, or if your tax liability on any day is \$100,000 or more. Show tax liability here, <b>not</b> deposits. (The IRS gets deposit data from FTD coupons or EFTPS.)						
<b>A. Daily Tax Liability—First Month of Quarter</b>						
1	8	15	22	29		
2	9	16	23	30		
3	10	17	24	31		
4	11	18	25			
5	12	19	26			
6	13	20	27			
7	14	21	28			
<b>A</b> Total tax liability for first month of quarter				<b>A</b>		
<b>B. Daily Tax Liability—Second Month of Quarter</b>						
1	8	15	22	29		
2	9	16	23	30		
3	10	17	24	31		
4	11	18	25			
5	12	19	26			
6	13	20	27			
7	14	21	28			
<b>B</b> Total tax liability for second month of quarter				<b>B</b>		
<b>C. Daily Tax Liability—Third Month of Quarter</b>						
1	8	15	22	29		
2	9	16	23	30		
3	10	17	24	31		
4	11	18	25			
5	12	19	26			
6	13	20	27			
7	14	21	28			
<b>C</b> Total tax liability for third month of quarter				<b>C</b>		
<b>D</b> Total for quarter (add lines A, B, and C). This should equal line 13 of Form 941 (or line 10 of Form 941-SS)				<b>D</b>		
For Paperwork Reduction Act Notice, see page 2. <span style="float: right;">Cat. No. 11967Q <b>Schedule B (Form 941) (Rev. 1-2002)</b></span>						

**General Instructions**

**Purpose of form.** Use Schedule B (Form 941) to report your **tax liability** (income tax withheld plus both employee and employer social security and Medicare taxes minus any advance earned income credit payments) on a daily basis. Form 941-SS filers report only employee and employer social security and Medicare taxes. **Do not** show Federal tax deposits. Deposit information is obtained from the deposit coupons (Form 8109) or from the Electronic Federal Tax Payment System (EFTPS).

**Example B.** Employer B is a semiweekly schedule depositor. It has paydays every other Friday. It accumulated a \$20,000 employment tax liability on each of the following pay dates: 1/12/01; 1/26/01; 2/9/01; 2/23/01; 3/9/01; and 3/23/01. Since Employer B is a semiweekly schedule depositor, it is required to record its tax liabilities on Schedule B (Form 941). Employer B must record the \$20,000 of liabilities on lines 12 and 26 of part A (First Month of Quarter); lines 9 and 23 of part B (Second Month of Quarter); and lines 9 and 23 of part C (Third Month of Quarter).

# Lesson 3

## Part II: Form 940, Employer's Annual Federal Unemployment (FUTA) Tax Return

### Introduction

The Federal Unemployment Tax Act (FUTA) provides for states and the federal government to cooperate in establishing and administering the unemployment tax program. The program provides for payments of unemployment compensation to workers who have lost their jobs.

The various states create the actual employment insurance systems. The federal government approves the state laws and pays the administrative costs of the state programs.

Under this dual system, the employer is first subject to a tax levied by the state. This tax then becomes a credit against a separate federal tax. However, you may be exempt from state tax but still have to pay the federal tax.

The federal unemployment (FUTA) tax is reported on Form 940, EMPLOYER'S ANNUAL FEDERAL UNEMPLOYMENT (FUTA) TAX RETURN or Form 940-EZ, EMPLOYER'S ANNUAL FEDERAL UNEMPLOYMENT (FUTA) TAX RETURN. Both forms cover one calendar year and are generally due by January 31 of the following year. (See Exhibits 3.10 and 3.11 on pages 3-26 through 3-31.)

### Objectives

At the end of this lesson, you will be able to:

1. Define employer, employee and wages subject to FUTA.
2. Figure the FUTA tax due.
3. Figure the deposits for FUTA taxes.
4. Complete Form 940-EZ.

### References

Publication 15, EMPLOYER'S TAX GUIDE (Circular E)  
Publication 15-A, EMPLOYER'S SUPPLEMENTAL TAX GUIDE



## Who Are Employers?

In general, you are an employer for FUTA tax purposes and must file and pay FUTA tax if, during the current *or* preceding year, you:

- paid wages of \$1,500 or more in any calendar quarter to employees (other than farm workers or household workers) **or**
- had one or more employees (other than farm workers or household workers) at any time in each of any 20 or more weeks (calendar).



The 20 weeks do not have to be consecutive. Count all regular, temporary and part-time employees, and count employees on vacation or sick leave.

You may be liable for the state unemployment tax and not liable for the FUTA tax. Conversely, you may be exempt from state tax and still have to pay the federal tax. The definition of employer under state laws may differ from the definition under federal law.

**Note:** *The term “employer” as used here refers to a person who is an employer for FUTA tax purposes only. It is possible not to be an employer for FUTA tax purposes and still be an employer for social security and Medicare tax purposes or for purposes of withholding income tax.*

## Who Are Employees?



The rules used of social security and Medicare tax also apply in determining who are common-law employees FUTA tax.

For FUTA tax, as for social security and Medicare taxes, there are statutory employees and non-employees in addition to common-law employees.

Refer to the charts of special classes of employment in Publication 15 to see which employees are covered by, or are exempt from, FUTA tax.

## What Are FUTA Wages?

As with wages for income tax withholding and social security and Medicare tax, FUTA wages generally include money and other forms of payment to employees. For other exceptions, refer to Publication 15 or Publication 15-A.

## Wages Not Paid In Money

If you pay your employees in some medium that is neither cash nor a readily negotiable instrument (such as a check), you are said to pay them “in kind.” Payments in kind may be in the form of goods, lodging, food, clothing or services. Generally, wages paid in kind are treated the same way as wages paid in money. The value of a wage payment in kind is its fair market price on the day the payment is made.

## Employee Taxes Paid by Employer

Generally, if you pay an employee’s liability for social security and Medicare taxes without deducting the tax from the employee’s pay, you must include the amount of the payment in the employee’s wages the FUTA tax.

## Figuring FUTA Tax

The FUTA tax is figured on the first \$7,000 in wages paid to each employee during the year. The tax is imposed on you as the employer. You must **not** collect it or deduct it from the wages you pay your employees.

The current FUTA tax rate is 6.2%. Generally, you can take a credit against your FUTA tax for amounts you paid into state unemployment funds. This credit cannot be more than 5.4% of taxable FUTA wages. If you are entitled to the maximum 5.4% credit, the FUTA tax rate after the credit is 0.8%.

## Example

In November 2001, you hired Alice Green, and paid her \$3,500 in wages before the year ended. All \$3,500 was subject to the FUTA tax. The first \$7,000 you pay her in 2002 is also subject to the tax. Alice’s total wages for 2002 reached \$7,000 in mid-March. None of the wages you pay her for the remainder of the year are subject to the FUTA tax.

In July, Alice quits her job, and you hire someone to replace her. The first \$7,000 you pay Alice’s replacement in 2002 is also subject to the FUTA tax.

## Credit for Contributions to States

Contributions are payments that a state requires an employer to make to its unemployment fund for the payment of unemployment benefits. However, contributions do **not** include:

- Any payments deducted or deductible from your employees’ pay.
- Penalties, interest or special administrative taxes not included in the contribution rate the state assigned to you.

- Voluntary contributions paid to get a lower assigned rate.

You may receive an additional credit if you have a state experience rate lower than 5.4% (.054). This applies even if your rate changes during the year. This additional credit is equal to the difference between actual payments and the amount you would have been required to pay at 5.4%.

The total credit allowable may not be more than 5.4% of taxable FUTA wages.



*Note: Credit for state contributions you make after the due date for filing Form 940 may not be more than 90% of the amount that would have been allowable if you had paid the amounts by the due date.*

## State Experience Rate

Your state experience rate is the rate at which the state taxes your payroll for state unemployment purposes. This rate may be adjusted from time to time based on the number and length of claims for unemployment compensation that your former employees make against the fund. If you do not know your rate, contact your state employment security agency.

If you have been granted an experience rate lower than the maximum credit of 5.4% by a state for all or part of the year, you are still allowed the full credit. However, you cannot take credit for any state taxes for which you are liable and do not pay.

## Successor Employer

If you acquire substantially all the property used in the business (or a unit of the business) of a previous employer who was subject to this tax, you may count, for purposes of the \$7,000 annual limit, the wages the previous employer paid during the year to the employees who continue to work for you.

## Depositing the Tax

If, at the end of any calendar quarter, you owe, but have not yet deposited, more than \$100 in FUTA tax, you must make a deposit by the last day of the next month. If the accumulated tax at the end of any of the first three quarters is \$100 or less, do not deposit the amount; instead, add it to the tax for the next quarter.

To figure your tax for each quarter, multiply .8% (.008) by the part of the first \$7,000 of each employee's annual FUTA tax wages that you paid during the quarter.

**When to Deposit**

Deposit the FUTA tax by the last day of the first month after the quarter ends.

If your liability for the fourth quarter (plus any amount not deposited from any earlier quarter) is over \$100, deposit the entire amount by the due date (January 31) of Form 940 or Form 940-EZ. If it is \$100 or less, you can either make a deposit or pay the tax with your Form 940 or 940-EZ by January 31.

**How to Deposit**

If your FUTA tax liability for any calendar quarter in 2002 is more than \$100 (including any FUTA tax carried forward from an earlier quarter), you must deposit the tax using EFTPS **or** in an authorized financial institution using Form 8109, FEDERAL TAX DEPOSIT COUPON.

**Example**

Tim Tower has two employees. In each quarter of 2002, George is paid wages of \$3,000 and Mark is paid wages of \$2,000. Tim's FUTA tax liability for each of the first and second quarters is \$40 ( $\$5,000 \times .008$ ). He is not required to deposit after the first or second quarter because his liability at the end of the second quarter is \$80 (not more than \$100). During the third quarter, Tim paid wages of \$3,000 subject to FUTA tax. Only \$1,000 of George's wages is taxable because \$6,000 was paid in the first two quarters. All of Mark's wages are taxable because he has not reached the \$7,000 level. Tim's tax liability for the third quarter is \$24 ( $\$3,000 \times .008$ ). His liability through the third quarter is \$104 (\$40 for each of the first and second quarters plus \$24 for the third). He must deposit \$104 by October 31, 2002.

In the fourth quarter, none of George's wages are subject to FUTA but \$1,000 of Mark's is taxable. Tim should pay \$8. ( $\$1,000 \times .008$ ) with Form 940 or 940-EZ.

**EXHIBIT 3.10 – BLANK FORM 940, EMPLOYER’S ANNUAL FEDERAL UNEMPLOYMENT (FUTA) TAX**

<p>Form <b>940</b></p> <p>Department of the Treasury Internal Revenue Service (99)</p>	<p><b>Employer’s Annual Federal Unemployment (FUTA) Tax Return</b></p> <p>▶ See separate Instructions for Form 940 for information on completing this form.</p>	<p>OMB No. 1545-0028</p> <p style="font-size: 24pt; font-weight: bold;">2002</p> <table border="1" style="width:100%; border-collapse: collapse;"> <tr><td>T</td><td></td></tr> <tr><td>FF</td><td></td></tr> <tr><td>FD</td><td></td></tr> <tr><td>FP</td><td></td></tr> <tr><td>I</td><td></td></tr> <tr><td>T</td><td></td></tr> </table>	T		FF		FD		FP		I		T														
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<p><b>You must complete this section.</b> ▶</p>	<p>Name (as distinguished from trade name) _____ Calendar year _____</p> <p>Trade name, if any _____</p> <p>Address and ZIP code _____ Employer identification number _____</p>																										
<p><b>A</b> Are you required to pay unemployment contributions to only one state? (If "No," skip questions B and C.).. <input type="checkbox"/> Yes <input type="checkbox"/> No</p> <p><b>B</b> Did you pay all state unemployment contributions by January 31, 2003? ((1) If you deposited your total FUTA tax when due, check "Yes" if you paid all state unemployment contributions by February 10, 2003. (2) If a 0% experience rate is granted, check "Yes." (3) If "No," skip question C.) . . . . . <input type="checkbox"/> Yes <input type="checkbox"/> No</p> <p><b>C</b> Were all wages that were taxable for FUTA tax also taxable for your state’s unemployment tax? . . . . . <input type="checkbox"/> Yes <input type="checkbox"/> No</p> <p>If you answered "No" to any of these questions, you must file Form 940. If you answered "Yes" to all the questions, you may file Form 940-EZ, which is a simplified version of Form 940. (Successor employers, see <b>Special credit for successor employers</b> on page 2 of the instructions.) You can get Form 940-EZ by calling 1-800-TAX-FORM (1-800-829-3676) or from the IRS Web Site at <a href="http://www.irs.gov">www.irs.gov</a>.</p>																											
<p><b>If you will not have to file returns in the future, check here</b> (see <b>Who Must File</b> in separate instructions) <b>and complete and sign the return</b> . . . . . <input type="checkbox"/></p> <p><b>If this is an Amended Return, check here</b> (see <b>Amended Returns</b> on page 2 of the separate instructions) . . . . . <input type="checkbox"/></p>																											
<p><b>Part I Computation of Taxable Wages</b></p> <table border="1" style="width:100%; border-collapse: collapse;"> <tr> <td style="width:60%;">1 Total payments (including payments shown on lines 2 and 3) during the calendar year for services of employees . . . . .</td> <td style="width:10%; text-align: center;">1</td> <td style="width:10%;"></td> <td style="width:10%;"></td> <td style="width:10%;"></td> </tr> <tr> <td>2 Exempt payments. (Explain all exempt payments, attaching additional sheets if necessary.) ▶</td> <td style="text-align: center;">2</td> <td style="background-color: #cccccc;"></td> <td style="background-color: #cccccc;"></td> <td style="background-color: #cccccc;"></td> </tr> <tr> <td>3 Payments of more than \$7,000 for services. Enter only amounts over the first \$7,000 paid to each employee. (see separate instructions) Do not include any exempt payments from line 2. The \$7,000 amount is the Federal wage base. Your state wage base may be different. <b>Do not use your state wage limitation.</b> . . . . .</td> <td style="text-align: center;">3</td> <td style="background-color: #cccccc;"></td> <td style="background-color: #cccccc;"></td> <td style="background-color: #cccccc;"></td> </tr> <tr> <td>4 Add lines 2 and 3 . . . . .</td> <td style="text-align: center;">4</td> <td></td> <td></td> <td></td> </tr> <tr> <td>5 <b>Total taxable wages</b> (subtract line 4 from line 1) . . . . . ▶</td> <td style="text-align: center;">5</td> <td></td> <td></td> <td></td> </tr> </table>			1 Total payments (including payments shown on lines 2 and 3) during the calendar year for services of employees . . . . .	1				2 Exempt payments. (Explain all exempt payments, attaching additional sheets if necessary.) ▶	2				3 Payments of more than \$7,000 for services. Enter only amounts over the first \$7,000 paid to each employee. (see separate instructions) Do not include any exempt payments from line 2. The \$7,000 amount is the Federal wage base. Your state wage base may be different. <b>Do not use your state wage limitation.</b> . . . . .	3				4 Add lines 2 and 3 . . . . .	4				5 <b>Total taxable wages</b> (subtract line 4 from line 1) . . . . . ▶	5			
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4 Add lines 2 and 3 . . . . .	4																										
5 <b>Total taxable wages</b> (subtract line 4 from line 1) . . . . . ▶	5																										

Be sure to complete both sides of this form, and sign in the space provided on the back.

For Privacy Act and Paperwork Reduction Act Notice, see separate instructions. ▼ **DETACH HERE** ▼ Cat. No. 112340 Form **940** (2002)

<p>Form <b>940-V</b></p> <p>Department of the Treasury Internal Revenue Service</p>	<p><b>Form 940 Payment Voucher</b></p> <p>Use this voucher only when making a payment with your return.</p>	<p>OMB No. 1545-0028</p> <p style="font-size: 24pt; font-weight: bold;">2002</p>			
<p>Complete boxes 1, 2, and 3. Do not send cash, and do not staple your payment to this voucher. Make your check or money order payable to the "United States Treasury." Be sure to enter your employer identification number, "Form 940," and "2002" on your payment.</p>					
<p>1 Enter your employer identification number.</p>	<p>2 <b>Enter the amount of your payment.</b> ▶</p> <table border="1" style="width:100%; border-collapse: collapse;"> <tr> <td style="width:70%;"></td> <td style="width:15%; text-align: center;">Dollars</td> <td style="width:15%; text-align: center;">Cents</td> </tr> </table>		Dollars	Cents	
	Dollars	Cents			
	<p>3 Enter your business name (individual name for sole proprietors).</p> <p>Enter your address.</p> <p>Enter your city, state, and ZIP code.</p>				

**EXHIBIT 3.10 – BLANK FORM 940, EMPLOYER’S ANNUAL FEDERAL UNEMPLOYMENT (FUTA) TAX RETURN, PAGE 2**

Form 940 (2002)

Page **2**

**Part II Tax Due or Refund**

- 1** Gross FUTA tax. (Multiply the wages from Part I, line 5, by .062) . . . . . **1**
- 2** Maximum credit. (Multiply the wages from Part I, line 5, by .054) . . . . . **2**
- 3** Computation of tentative credit (**Note: All taxpayers must complete the applicable columns.**)

(a) Name of state	(b) State reporting number(s) as shown on employer's state contribution returns	(c) Taxable payroll (as defined in state act)	(d) State experience rate period		(e) State ex- perience rate	(f) Contributions if rate had been 5.4% (col. (c) x .054)	(g) Contributions payable at experience rate (col. (c) x col. (e))	(h) Additional credit (col. (f) minus col.(g)) If 0 or less, enter -0-	(i) Contributions paid to state by 940 due date
			From	To					
<b>3a</b> Totals . . . ▶									

**3b** Total tentative credit (add line 3a, columns (h) and (i) only—for late payments, also see the instructions for Part II, line 6) . . . . . **3b**

- 4** **5** **6** **Credit:** Enter the smaller of the amount from Part II, line 2 or line 3b; or the amount from the worksheet on page 5 of the separate instructions . . . . . **6**
- 7** **Total FUTA tax** (subtract line 6 from line 1). If the result is over \$100, also complete Part III . . . . . **7**
- 8** **Total FUTA tax** deposited for the year, including any overpayment applied from a prior year . . . . . **8**
- 9** **Balance due** (subtract line 8 from line 7). Pay to the "United States Treasury." If you owe more than \$100, see **Depositing FUTA Tax** on page 3 of the separate instructions . . . . . **9**
- 10** **Overpayment** (subtract line 7 from line 8). Check if it is to be:  **Applied to next return** or  **Refunded** . . . . . **10**

**Part III Record of Quarterly Federal Unemployment Tax Liability** (Do not include state liability.) **Complete only if line 7 is over \$100.** See page 6 of the separate instructions.

Quarter	First (Jan. 1–Mar. 31)	Second (Apr. 1–June 30)	Third (July 1–Sept. 30)	Fourth (Oct. 1–Dec. 31)	Total for year
Liability for quarter					

**Third Party Designee** Do you want to allow another person to discuss this return with the IRS (see instructions page 6)?  **Yes.** Complete the following.  **No**

Designee's name ▶ Phone no. ▶ ( ) Personal identification number (PIN) ▶

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and, to the best of my knowledge and belief, it is true, correct, and complete, and that no part of any payment made to a state unemployment fund claimed as a credit was, or is to be, deducted from the payments to employees.

Signature ▶ Title (Owner, etc.) ▶ Date ▶



Form **940** (2002)

**EXHIBIT 3.11 – BLANK FORM 940-EZ, EMPLOYER’S ANNUAL FEDERAL UNEMPLOYMENT (FUTA) TAX RETURN**

Form **940-EZ** | **Employer’s Annual Federal Unemployment (FUTA) Tax Return** | OMB No. 1545-1110

Department of the Treasury Internal Revenue Service (99) | ▶ See separate instructions for Form 940-EZ for information on completing this form. | **2002**

Name (as distinguished from trade name) \_\_\_\_\_ Calendar year \_\_\_\_\_

Trade name, if any \_\_\_\_\_

Address and ZIP code \_\_\_\_\_ Employer identification number \_\_\_\_\_

**You must complete this section.** ▶

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Answer the questions under **Who May Use Form 940-EZ** on page 2. If you cannot use Form 940-EZ, you must use Form 940.

**A** Enter the amount of contributions paid to your state unemployment fund. (See separate instructions) . . . ▶ \$ \_\_\_\_\_

**B** (1) Enter the name of the state where you have to pay contributions . . . ▶ \_\_\_\_\_  
 (2) Enter your state reporting number as shown on your state unemployment tax return ▶ \_\_\_\_\_

If you will not have to file returns in the future, check here (see **Who Must File** in separate instructions) and complete and sign the return. ▶

If this is an Amended Return, check here (see **Amended Returns** on page 2 of the separate instructions) . . . ▶

**Part I Taxable Wages and FUTA Tax**

1	Total payments (including payments shown on lines 2 and 3) during the calendar year for services of employees	1	
2	Exempt payments. (Explain all exempt payments, attaching additional sheets if necessary.) ▶	2	
3	Payments of more than \$7,000 for services. Enter only amounts over the first \$7,000 paid to each employee. (see separate instructions)	3	
4	Add lines 2 and 3	4	
5	<b>Total taxable wages</b> (subtract line 4 from line 1)	5	
6	<b>FUTA tax.</b> Multiply the wages on line 5 by .008 and enter here. (If the result is over \$100, also complete Part II.)	6	
7	Total FUTA tax deposited for the year, including any overpayment applied from a prior year	7	
8	<b>Balance due</b> (subtract line 7 from line 6). Pay to the "United States Treasury." If you owe more than \$100, see <b>Depositing FUTA tax</b> in separate instructions.	8	
9	<b>Overpayment</b> (subtract line 6 from line 7). Check if it is to be: <input type="checkbox"/> Applied to next return or <input type="checkbox"/> Refunded ▶	9	

**Part II Record of Quarterly Federal Unemployment Tax Liability** (Do not include state liability.) Complete only if line 6 is over \$100.

Quarter	First (Jan. 1 – Mar. 31)	Second (Apr. 1 – June 30)	Third (July 1 – Sept. 30)	Fourth (Oct. 1 – Dec. 31)	Total for year
Liability for quarter					

**Third Party Designee** Do you want to allow another person to discuss this return with the IRS (see instructions page 5)?  Yes. Complete the following.  No

Designee's name \_\_\_\_\_ Phone no. \_\_\_\_\_ ( ) \_\_\_\_\_ Personal identification number (PIN) \_\_\_\_\_

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and, to the best of my knowledge and belief, it is true, correct, and complete, and that no part of any payment made to a state unemployment fund claimed as a credit was, or is to be, deducted from the payments to employees.

Signature ▶ \_\_\_\_\_ Title (Owner, etc.) ▶ \_\_\_\_\_ Date ▶ \_\_\_\_\_

For Privacy Act and Paperwork Reduction Act Notice, see separate instructions. ▼ DETACH HERE ▼ Cat. No. 10983G Form 940-EZ (2002)

Form **940-EZ(V)** | **Form 940-EZ Payment Voucher** | OMB No. 1545-1110

Department of the Treasury Internal Revenue Service | Use this voucher only when making a payment with your return. | **2002**

Complete boxes 1, 2, and 3. Do not send cash, and do not staple your payment to this voucher. Make your check or money order payable to the "United States Treasury." Be sure to enter your employer identification number, "Form 940-EZ," and "2002" on your payment.

1 Enter your employer identification number. \_\_\_\_\_

2	<b>Enter the amount of your payment.</b> ▶	Dollars	Cents
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3 Enter your business name (individual name for sole proprietors). \_\_\_\_\_

Enter your address. \_\_\_\_\_

Enter your city, state, and ZIP code. \_\_\_\_\_

## Forms 940 and 940-EZ Filing

You can file Form 940-EZ instead of Form 940 if you:

- paid unemployment taxes (“contributions”) to only one state,
- paid all state unemployment taxes by January 31, 2003 (February 11, if you deposited all FUTA tax when due) and
- all wages that were taxable for FUTA tax purposes were also taxable for your state’s unemployment tax.

For example, if you paid wages to corporate officers (these wages are subject to FUTA tax) in a state that exempts these wages from its unemployment taxes, you cannot use Form 940-EZ.

### Form 940-EZ

#### Lines A and B

You must complete lines A and B and Part I. If your FUTA tax (line 6) is over \$100, you must also complete Part II.

**Line A.**

Enter the amount of your state unemployment contributions. If you are lucky enough to have been given a state experience rate of 0% enter “0% rate” in the space.

**Line B (1).**

Enter the state where you pay unemployment contributions.

**Line B (2).**

Enter your state reporting number.

#### Part I. Taxable Wages And FUTA Tax

**Line 1.**

Enter the total payments made during the year for services of employees.

**Line 2.**

Enter payments that are exempt for FUTA purposes, see Publication 15 (under Special Rules for Various Types of Services and Payments). Do not enter payments over \$7,000 for each employee.

**Line 3.**

Enter the amount of taxable payments that were over the \$7,000 you paid each employee.



**Line 6.**

Compute the FUTA tax by multiplying the wages on Line 5 by .008.

**Line 7.**

FUTA tax deposited.

**Line 8.**

Balance due.

**Line 9.**

Overpayment.

## Part II. Record of Quarterly FUTA Tax Liability

Complete this part only if your FUTA tax on line 6 is over \$100. Your quarterly FUTA tax liability is figured by multiplying the wages subject to FUTA tax within the \$7,000 limit by .008. The total **must** match line 6 in part I.

Remember, this is your tax liability based on when you paid the wages and **not** on when the deposits were made.

## Example of Completed Form 940-EZ

Sue Martin owner of Martin's Fabric Shop has two employees, whom she paid each Friday. She meets all the filing requirements for Form 940-EZ. She made contributions of \$352.00 to the state of Virginia and her state unemployment number is VA94371. Form 940-EZ has been completed using the following information (See Exhibit 3.12 on page 3-33):

					
Employee	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>	Total
John	\$3,600	\$3,900	\$3,900	\$4,200	\$15,600
Mary	\$5,400	\$5,850	\$5,850	\$6,300	\$23,400

EXHIBIT 3.12 - FORM 940-EZ, SUE MARTIN EXAMPLE

Form <b>940-EZ</b> <small>Department of the Treasury Internal Revenue Service (99)</small>	<b>Employer's Annual Federal Unemployment (FUTA) Tax Return</b>	OMB No. 1545-1110  <div style="font-size: 2em; font-weight: bold;">2002</div>												
▶ See separate instructions for Form 940-EZ for information on completing this form.		<table border="1" style="width:100%; border-collapse: collapse;"> <tr><td>T</td><td></td></tr> <tr><td>FF</td><td></td></tr> <tr><td>FD</td><td></td></tr> <tr><td>FP</td><td></td></tr> <tr><td>I</td><td></td></tr> <tr><td>T</td><td></td></tr> </table>	T		FF		FD		FP		I		T	
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You must complete this section. ▶	Name (as distinguished from trade name) <b>SUE MARTIN</b> Calendar year <b>2002</b> Trade name, if any <b>MARTIN'S FABRIC SHOP</b> Address and ZIP code <b>1070 MOUNTAIN ST., SOUTH PORT, VA 27711</b> Employer identification number <b>22-1122234</b>													

Answer the questions under **Who May Use Form 940-EZ** on page 2. If you cannot use Form 940-EZ, you must use Form 940.

**A** Enter the amount of contributions paid to your state unemployment fund. (see separate instructions) . . . . . \$ **352**

**B** (1) Enter the name of the state where you have to pay contributions . . . . . **VIRGINIA**

(2) Enter your state reporting number as shown on your state unemployment tax return ▶ **VA 94371**

If you will not have to file returns in the future, check here (see **Who Must File** in separate instructions) and complete and sign the return. ▶

If this is an Amended Return, check here (see **Amended Returns** on page 2 of the separate instructions) . . . . . ▶

**Part I Taxable Wages and FUTA Tax**

1 Total payments (including payments shown on lines 2 and 3) during the calendar year for services of employees	1	39,000	00
2 Exempt payments. (Explain all exempt payments, attaching additional sheets if necessary.) ▶	2		
3 Payments of more than \$7,000 for services. Enter only amounts over the first \$7,000 paid to each employee. (see separate instructions)	3	25,000	00
4 Add lines 2 and 3	4	25,000	00
5 Total taxable wages (subtract line 4 from line 1)	5	14,000	00
6 FUTA tax. Multiply the wages on line 5 by .008 and enter here. (If the result is over \$100, also complete Part II.)	6	112	00
7 Total FUTA tax deposited for the year, including any overpayment applied from a prior year	7	112	00
8 Balance due (subtract line 7 from line 6). Pay to the "United States Treasury."	8		
9 Overpayment (subtract line 6 from line 7). Check if it is to be: <input type="checkbox"/> Applied to next return or <input type="checkbox"/> Refunded ▶	9		

**Part II Record of Quarterly Federal Unemployment Tax Liability** (Do not include state liability.) Complete only if line 6 is over \$100.

Quarter	First (Jan. 1 – Mar. 31)	Second (Apr. 1 – June 30)	Third (July 1 – Sept. 30)	Fourth (Oct. 1 – Dec. 31)	Total for year
Liability for quarter	72.00	40.00			112.00

**Third Party Designee** Do you want to allow another person to discuss this return with the IRS (see instructions page 5)?  Yes. Complete the following.  No

Designee's name ▶ \_\_\_\_\_ Phone no. ▶ ( ) \_\_\_\_\_ Personal identification number (PIN) ▶ \_\_\_\_\_

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and, to the best of my knowledge and belief, it is true, correct, and complete, and that no part of any payment made to a state unemployment fund claimed as a credit was, or is to be, deducted from the payments to employees.

Signature ▶ \_\_\_\_\_ Title (Owner, etc.) ▶ \_\_\_\_\_ Date ▶ \_\_\_\_\_

For Privacy Act and Paperwork Reduction Act Notice, see separate instructions. ▼ DETACH HERE ▼ Cat. No. 10983G Form 940-EZ (2002)

Form <b>940-EZ(V)</b> <small>Department of the Treasury Internal Revenue Service</small>	<b>Form 940-EZ Payment Voucher</b>	OMB No. 1545-1110  <div style="font-size: 2em; font-weight: bold;">2002</div>			
Use this voucher only when making a payment with your return.					
Complete boxes 1, 2, and 3. Do not send cash, and do not staple your payment to this voucher. Make your check or money order payable to the "United States Treasury." Be sure to enter your employer identification number, "Form 940-EZ," and "2002" on your payment.					
1 Enter your employer identification number.		<table border="1" style="width:100%; border-collapse: collapse;"> <tr> <td style="width:60%;"></td> <td style="width:20%; text-align: center;">Dollars</td> <td style="width:20%; text-align: center;">Cents</td> </tr> </table>		Dollars	Cents
	Dollars	Cents			
	2	Enter the amount of your payment. ▶			
	3	Enter your business name (individual name for sole proprietors). Enter your address. Enter your city, state, and ZIP code.			

**EXHIBIT 3.13 – FORM 940, APPLIED FOR (DATE) EXAMPLE**

Form **940**

Department of the Treasury  
Internal Revenue Service (99)

**Employer’s Annual Federal  
Unemployment (FUTA) Tax Return**

▶ See separate Instructions for Form 940 for information on completing this form.

OMB No. 1545-0028

**2002**

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Name (as distinguished from trade name)
 Calendar year

Trade name, if any

Address and ZIP code

**APPLIED FOR - DATE**

Employer identification number

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**You must complete this section.** ▶

**Tips for  
Completing  
Forms 940  
or 940-EZ**

Always use a preaddressed form if available. This insures faster and more accurate processing. However, if your preaddressed form is not available, do not delay filing because you could be charged a late filing penalty. Using a current year form, enter your name, trade name, address, ZIP code and your EIN. If you have applied for an EIN, but have not received it, write "Applied for" and the date you applied in the space provided for the number (See Exhibit 3.13 above.)

**Summary**

In this lesson you learned who must pay FUTA tax, what wages are subject to this tax, how to figure the amount of FUTA tax due and when the tax must be deposited. You also learned how to complete Form 940-EZ. Important points to remember include:

- when Form 940 or 940-EZ is due,
- what the deposit requirements are **and**
- that only employers pay FUTA tax.

## Exercises

### Exercise 1

Mr. Wilson opened a business in January 2002 and hired six-employees. In the first quarter he paid the employees each week for 13 weeks. Use the following information to determine:

- (A) How much of the total wages is subject to FUTA tax? \$ \_\_\_\_
- (B) What is the first quarter FUTA tax liability? \$ \_\_\_\_\_
- (C) When is the deposit due date? \_\_\_\_\_

Mr. Wilson's Business	
Employee	Wages Paid in Quarter
R. Riding	\$ 4,500
M. Lamb	8,100
J. Nimble	3,400
C. Moon	5,600
C. Fiddle	4,900
P. Son	5,200
Total Wages	\$31,700

Assume that the same facts are true for the second quarter (that is, there are 13 paydays; each employee's wages remain the same and no new employees are hired). Use the information in the previous table to determine:

- (D) How much of the total wages is subject to FUTA tax?  
\$ \_\_\_\_\_
- (E) What is the second quarter FUTA tax liability? \$ \_\_\_\_\_
- (F) Is a deposit due?  YES.  NO
- (G) When an employer pays state contributions after the due date (or extended due date) of Form 940, the credit for the state contributions is \_\_\_\_% of the amount that would be allowed if the employer had paid the state contributions by the due date.

*(Answers are found on page A-6.)*

**Exercise 2**

Complete Form 940-EZ for ACME Inc., using Exhibit 3.14 - BLANK FORM 940-EZ FOR EXERCISE 2 on page 3-37 and the following information:

State reporting number: 12345

State taxable payroll: \$18,200

Experience rate: 2.7% from January 1 to December 31, 2002.

During 2002 and before the date of Form 940-EZ, ACME paid \$491.40 to Michigan for unemployment tax.

ACME, Inc.,  
EIN: 10-7654321  
123 First St.  
Cedar, MI 49621

ACME, Inc., Deposits					
Employee	Annual Wage	Quarter			
		1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>
Ben Wood	\$12,600.00	\$3,150.00	\$2,850.00	\$1,000.00	-0-
Mary Birch	9,200.00	2,300.00	2,300.00	1,400.00	\$1,000.00
John Cane	4,200.00	1,050.00	1,050.00	1,050.00	1,050.00
Totals	26,000.00	6,500.00	6,200.00	3,450.00	2,050.00
x.008		\$52.00	49.60	27.60	16.40
Cumulative		\$52.00	101.60	27.60	44.00
Amount Deposited		-0-	101.60	-0-	-0-

A. When must ACME make deposit(s)? \_\_\_\_\_

B. How much must be deposited? \$ \_\_\_\_\_

C. How much must be paid with the return? \$ \_\_\_\_\_

*(Answers are found on pages A-6 and A-7.)*

EXHIBIT 3.14 - BLANK FORM 940-EZ FOR EXERCISE 2

Form **940-EZ** | **Employer's Annual Federal Unemployment (FUTA) Tax Return** | OMB No. 1545-1110

Department of the Treasury Internal Revenue Service (99) | **2002**

▶ See separate instructions for Form 940-EZ for information on completing this form.

Name (as distinguished from trade name) \_\_\_\_\_ Calendar year \_\_\_\_\_

Trade name, if any \_\_\_\_\_

Address and ZIP code \_\_\_\_\_ Employer identification number \_\_\_\_\_

**You must complete this section.**

Answer the questions under **Who May Use Form 940-EZ** on page 2. If you cannot use Form 940-EZ, you must use Form 940.

**A** Enter the amount of contributions paid to your state unemployment fund. (See separate instructions) . . . ▶ \$ \_\_\_\_\_

**B** (1) Enter the name of the state where you have to pay contributions . . . ▶ \_\_\_\_\_  
 (2) Enter your state reporting number as shown on your state unemployment tax return ▶ \_\_\_\_\_

If you will not have to file returns in the future, check here (see **Who Must File** in separate instructions) and complete and sign the return. ▶

If this is an Amended Return, check here (see **Amended Returns** on page 2 of the separate instructions) . . . ▶

**Part I Taxable Wages and FUTA Tax**

1	Total payments (including payments shown on lines 2 and 3) during the calendar year for services of employees	1	
2	Exempt payments. (Explain all exempt payments, attaching additional sheets if necessary.) ▶	2	
3	Payments of more than \$7,000 for services. Enter only amounts over the first \$7,000 paid to each employee. (See separate instructions)	3	
4	Add lines 2 and 3	4	
5	<b>Total taxable wages</b> (subtract line 4 from line 1)	5	
6	<b>FUTA tax.</b> Multiply the wages on line 5 by .008 and enter here. (If the result is over \$100, also complete Part II.)	6	
7	Total FUTA tax deposited for the year, including any overpayment applied from a prior year	7	
8	<b>Balance due</b> (subtract line 7 from line 6). Pay to the "United States Treasury." If you owe more than \$100, see <b>Depositing FUTA tax</b> in separate instructions.	8	
9	<b>Overpayment</b> (subtract line 6 from line 7). Check if it is to be: <input type="checkbox"/> Applied to next return or <input type="checkbox"/> Refunded ▶	9	

**Part II Record of Quarterly Federal Unemployment Tax Liability** (Do not include state liability.) Complete only if line 6 is over \$100.

Quarter	First (Jan. 1 – Mar. 31)	Second (Apr. 1 – June 30)	Third (July 1 – Sept. 30)	Fourth (Oct. 1 – Dec. 31)	Total for year
Liability for quarter					

**Third Party Designee** Do you want to allow another person to discuss this return with the IRS (see instructions page 5)?  Yes. Complete the following.  No

Designee's name \_\_\_\_\_ Phone no. \_\_\_\_\_ Personal identification number (PIN) \_\_\_\_\_

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and, to the best of my knowledge and belief, it is true, correct, and complete, and that no part of any payment made to a state unemployment fund claimed as a credit was, or is to be, deducted from the payments to employees.

Signature ▶ \_\_\_\_\_ Title (Owner, etc.) ▶ \_\_\_\_\_ Date ▶ \_\_\_\_\_

For Privacy Act and Paperwork Reduction Act Notice, see separate instructions. ▼ DETACH HERE ▼ Cat. No. 10983G Form 940-EZ (2002)

Form **940-EZ(V)** | **Form 940-EZ Payment Voucher** | OMB No. 1545-1110

Department of the Treasury Internal Revenue Service | **2002**

Use this voucher only when making a payment with your return.

Complete boxes 1, 2, and 3. Do not send cash, and do not staple your payment to this voucher. Make your check or money order payable to the "United States Treasury." Be sure to enter your employer identification number, "Form 940-EZ," and "2002" on your payment.

1 Enter your employer identification number. \_\_\_\_\_

2 Enter the amount of your payment. ▶ Dollars \_\_\_\_\_ Cents \_\_\_\_\_

3 Enter your business name (individual name for sole proprietors).  
 Enter your address. \_\_\_\_\_  
 Enter your city, state, and ZIP code. \_\_\_\_\_

Notes

# Lesson 4

## Business Use of Your Home

### Introduction

The purpose of this lesson is to provide information on figuring and claiming the deduction for *business use of your home*. The term **home** can include a house, apartment, condominium, mobile home or boat. It also includes structures on the property, such as an unattached garage, studio, barn or greenhouse.



### Objectives

1. Determine if you are eligible for the *business use of the home* deduction.
2. Complete Form 8829, EXPENSES FOR THE BUSINESS USE OF YOUR HOME.



## Qualifying for a Deduction



To deduct expenses related to the business use of part of your home, you must meet specific requirements. Even then, the deduction may be limited. To qualify to claim expenses for the *business use of your home*, you must meet the following tests:

- your use of the business part of your home must be:
  - exclusive (see Exceptions to exclusive use, later),
  - regular and
  - for your business, and
- the business part of your home must be one of the following:
  - your principal place of business,
  - a place where you meet with patients, clients or customers in the normal course of your business, or
  - a separate structure (not attached to your home) you use in connection with your business.

## Exclusive Use

To qualify under the exclusive use test, you must use a specific area of your home **only** for your trade or business. The area used for business can be a room or other separately identifiable space. The space does not need to be marked off by a permanent partition.

You do **not** meet the requirements of the exclusive use test if you use the area in question both for business and for personal purposes.

**Example:** You are an attorney and use a den in your home to write legal briefs and prepare client tax returns. Your family also uses the den for recreation. Since the den is not used exclusively in your profession, you **cannot** claim a business deduction for its use.

## Exceptions to Exclusive Use

You do **not** have to meet the exclusive use test if:

- you use part of your home for the storage of inventory or product samples, or
- you use part of your home as a day-care facility.

## Regular Use

To qualify under the regular use test, you must use a specific area of your home for business on a continuing basis. You do not meet



## Principal Place of Business

the test if your business use of the area is only occasional or incidental, even if you do not use that area for any other purpose.

You can have more than one business location, including your home, for a single trade or business. One way to qualify to deduct the expenses for the *business use of your home* is if your home is your principal place of business. To determine this, you must consider all of the facts and circumstances.

Your home office will qualify as your principal place of business for deducting expenses for its use if:

- you use it exclusively and regularly for administrative or management activities of your trade or business and
- you have no other fixed location where you conduct substantial administrative or management activities of your trade or business.

The following activities that are administrative or managerial in nature:

- billing customers,
- keeping books and records,
- ordering supplies,
- setting up appointments and
- forwarding orders or writing reports.

The following activities will **not** disqualify your home office as your principal place of business:

- employing others to conduct your administrative or management activities at locations other than your home,
- conducting administrative or management activities at places that are not fixed locations of your business, such as in a car or a hotel room,
- occasionally conducting minimal administrative or management activities at a fixed location outside your home,
- conducting substantial nonadministrative or nonmanagement business activities at a fixed location outside your home and
- having suitable space to conduct administrative or management activities outside your home, but choosing to use your home office for those activities instead.

**Example A:** Jon is a self-employed plumber. Most of Jon's time is

spent at customers' homes and offices installing and repairing plumbing. He has a small office in his home that he uses exclusively and regularly for the administrative or management details of his

business, such as phoning customers, ordering supplies and keeping his books. Jon does not do his own billing. He uses a local bookkeeping service to bill his customers.

Jon's home office qualifies as his principal place of business for deducting expenses for its use. He uses the home office for the administrative or managerial activities of his plumbing business and he has no other fixed location where he conducts these administrative or managerial activities. His choice to have his billing done by another company does not disqualify his home office as his principal place of business. Because he meets all the qualifications, including principal place of business, he can deduct expenses (to the extent of the deduction limit) for the *business use of his home*.

**Example B:** Clyde is a self-employed anesthesiologist. He spends the majority of his time administering anesthesia and postoperative care in three local hospitals. One of the hospitals provides him with a small-shared office where he could conduct administrative or management activities. Clyde does not use the office the hospital provides. He uses a room in his home, that he has converted, as an office. He uses this room exclusively and regularly to conduct all the following activities:



- contacting patients, surgeons and hospitals regarding scheduling,
- preparing for treatments and presentations,
- maintaining billing records and patient logs,
- satisfying continuing medical education requirements and
- reading medical journals and books.

Clyde's home office qualifies as his principal place of business for deducting expenses for its use. He conducts administrative or management activities there for his business as an anesthesiologist. He has no other fixed location where he conducts administrative or management activities for this business. His choice to use his home office instead of one provided by the hospital does not disqualify his home office as his principal place of business. His performance of

substantial nonadministrative or nonmanagement activities at fixed locations outside his home also does not disqualify his home office as his principal place of business. Because he meets all the qualifications, including principal place of business, he can deduct expenses (to the extent of the deduction limit) for the *business use of his home*.

## Meeting Place for Customers



If you do not meet the principal place of business test, your home office may qualify if you meet or deal with patients, clients or customers in your home in the normal course of your business, even though you also carry on business at another location. You can deduct your expenses for the part of your home used exclusively and regularly for business if:

- you physically meet with patients, clients or customers at your home **and**
- the use of your home is substantial and integral to the conduct of your business.

Using your home for occasional meetings and telephone calls will not qualify you to deduct expenses for the business use of your home.

## Separate Structure

You can deduct expenses for a separate freestanding structure, such as a studio, garage, storage shed or barn, if you use it exclusively and regularly for your business. The structure does not have to be your principal place of business or a place where you meet patients, clients or customers.

## Business Percentage

Most expenses related to the *business use of your home* are limited to the percentage of your home used for business (business percentage).

To find the business percentage, compare the size of the part of your home that you use for business to your whole house. You can use any reasonable method to determine the business percentage. The following are two commonly used methods for figuring the percentage.

### Area Method



Divide the area used for business by the total area of your home.

**Example:** Your office is 240 square feet. Your home is 1200 square feet. Your office is 20% (240/1200) of the total area of your home. Your business percentage is 20%.

## Number-of-Rooms Method

Divide the number of rooms used for business by the total number of rooms in your home. You can use this method if the rooms in your home are all about the same size.

**Example:** Peggy has an art studio in her home. She is allowed to take a deduction for the *business use of her home*. The rooms in her house are all about the same size. There are ten rooms and she uses one for a studio. Her business-use percentage is 10%.

**Note:** Use lines 1-7 of Form 8829, *EXPENSES FOR BUSINESS USE OF YOUR HOME*, to figure your business percentage.

## Types of Expenses

There are two types of expenses related to using your home for business.

1. Expenses related to the business activity in the home but not to the use of the home itself.
2. Expenses for the *business use of the home*.

Expenses for the *business use of the home* are divided into three categories.

1. Direct expenses
2. Indirect expenses
3. Unrelated expenses

## Expenses Not Related to Business Use of the Home

Business expenses related to the business activity in the home but not to the use of the home itself are deductible in full on Schedule C (Form 1040) or Schedule F (Form 1040). These expenses are not limited to the *business use of the home* percentage or the deduction limit (discussed later). Examples of some of these expenses include the following:

- advertising,
- business taxes,
- car and truck expenses,
- salaries,
- supplies and
- travel.

## Expenses for Business Use of Your Home

You must divide the expenses of operating your home between personal and business use. The part of a home operating expense that you can use to figure your deduction depends on:

- whether the expense is direct, indirect or unrelated **and**
- the percentage of your home that is used for business.

### Direct Expenses

Expenses only for the business part of your home are generally deductible in full unless subject to the deduction limit, discussed later.

*Example:* Painting or repairs only in the area used for business.

### Indirect Expenses

Expenses for running your entire home are deductible based on the percentage of your home used for business. They may also be subject to the deduction limit, discussed later.



*Examples:* Insurance, utilities and general repairs.

### Unrelated Expenses

Expenses for the parts of your home not used for business are **not** deductible; (i.e. lawn care, painting a room not used for business).

*Example:* Jeff is allowed to take a deduction for the *business use of his home*. He has the following expenses:

Landscaping	\$1,500
Painting the business office	\$700
Utilities for the entire house	\$1,060
Repairs to the roof of the house	\$500
Repairs to the business office	\$100
Painting the bedroom	\$400

Painting the bedroom and landscaping are unrelated expenses. They cannot be deducted. The painting and repairs to the office are direct expenses and can be deducted in full. The repairs to the roof and utilities are indirect expenses. They are divided

## Examples of Expenses

between business and personal parts of the house. The business part is deductible.

Certain expenses are deductible whether or not you use your home for business. However, if you qualify to claim *business use of the home* expenses, you can use the business part of these expenses to figure your business use of the home deduction.

These expenses are:

- real estate taxes,
- deductible mortgage interest and
- casualty losses.

Other expenses are deductible only if you use your home for business. These expenses generally include (but are not limited to):

- insurance,
- rent,
- repairs,
- utilities and services and
- depreciation on your home.

**Real Estate Taxes:** To figure the business part of your real estate taxes, multiply the real estate taxes paid by the percentage of your home used for business.

**Deductible Mortgage Interest:** To figure the business part of your deductible mortgage interest, multiply this interest by the percentage of your home used for business.

**Casualty Losses:** If you have a casualty loss on your home that you use for business, treat the casualty loss as a direct expense, an indirect expense or an unrelated expense, depending on the property affected. If the loss is on a part of the property used for both business and personal purposes, use only the business portion to figure the deduction.

**Insurance:** You can deduct the cost of insurance that covers the business part of your home. However, if your insurance premium gives you coverage for a period that extends past the end of your tax year, you can deduct only the business percentage of the part of the premium that gives you coverage for your tax year.

**Rent:** If you rent, rather than own, a home and meet the requirements for *business use of the home*, you can deduct part of the rent you pay. To figure your deduction multiply your rent payments

by the percentage of your home used for business.

**Repairs:** The cost of repairs and supplies that relate to your business, including labor (other than your own labor), is a deductible expense. For example, a furnace repair benefits the entire home. If you use 10% of your home for business, you can deduct 10% of the cost of the furnace repair.

**Utilities and services:** You may deduct the business portion of your utilities and services, such as gas, electricity, trash removal and cleaning services. Generally, the amount deductible is the business-use percentage multiplied by the utility expense. The basic local telephone service charge, including taxes, for the first telephone line into your home is not deductible. However, charges for business long-distance phone calls on that line, as well as, the cost of a second line into your home used exclusively for business, are deductible business expenses. Deduct these charges on either Schedule C (Form 1040) or Schedule F (Form 1040). They are not part of your home office deduction.

**Depreciation:** Some expenses cannot be deducted all at once. The cost of any business property that lasts for more than one year must generally be deducted over a number of years. The annual expense is called depreciation. Depreciation reflects the reduction in value of the property.

To calculate depreciation on the business part of your home, you need to determine the depreciable basis of your home. Generally the depreciable basis of your home will be the lesser of:

1. the fair market value of your home (excluding land) on the date you first use it for business **or**
2. the purchase price (excluding land) plus any major improvements you made and minus any casualty losses or other changes to basis.

To determine how much of the depreciable basis you can use to compute your depreciation deduction, multiply the depreciable basis by the business-use percentage.

**Example:** Barry owns an accounting service. He uses 10% of his home as a business office. When Barry started his business, his home was worth \$60,000. The home cost \$50,000 and the land \$10,000. The depreciable basis of the home is \$50,000. The depreciable basis of the business part of the home is \$5,000 (\$50,000 depreciable basis multiplied by 10% business-use

percentage).

For information on how to calculate depreciation, see INSTRUCTIONS TO FORM 8829 or IRS Publication 946, HOW TO DEPRECIATE PROPERTY.

**Example:** The following example shows how to compute the business percentage of the various expenses using Form 8829, EXPENSES FOR BUSINESS USE OF YOUR HOME.

Renee operates a private detective agency in her home. She is allowed to take a deduction for expenses related to the *business use of the home*. Renee’s business-use percentage is 20 percent. She has the following expenses:

Real estate taxes	\$1000
Dues	\$50
Repairs to the floor of the office	\$200
Utilities	\$800
Transportation expenses	\$150
Insurance premiums on entire house	\$600
Mortgage Interest	\$700
Depreciation on entire house	\$700
Advertising	\$100
Painting the office	\$400
Business cards	\$50
Roof repair	\$100

Exhibit 4.1 on page 4-11 shows lines 9-30, Form 8829, EXPENSES FOR BUSINESS USE OF YOUR HOME, for Renee. Dues, transportation, advertising and business cards are expenses related to the business activity in the home but not to the *business use of the home* itself.



**EXHIBIT 4.1 - EXPENSES RELATED TO BUSINESS USE OF THE HOME, FOR RENEE EXAMPLE**

Form <b>8829</b> Department of the Treasury Internal Revenue Service (99)	<b>Expenses for Business Use of Your Home</b> ▶ File only with Schedule C (Form 1040). Use a separate Form 8829 for each home you used for business during the year. ▶ See separate instructions.	OMB No. 1545-1266 <b>2002</b> Attachment Sequence No. 66
Name(s) of proprietor(s) <b>RENEE</b>		Your social security number <b>111   11   1122</b>
<b>Part I Part of Your Home Used for Business</b>		
1	Area used regularly and exclusively for business, regularly for day care, or for storage of inventory or product samples (see instructions)	1
2	Total area of home	2
3	Divide line 1 by line 2. Enter the result as a percentage	3 %
• For day-care facilities not used exclusively for business, also complete lines 4-6. • All others, skip lines 4-6 and enter the amount from line 3 on line 7.		
4	Multiply days used for day care during year by hours used per day	4 hr.
5	Total hours available for use during the year (365 days × 24 hours) (see instructions)	5 8,760 hr.
6	Divide line 4 by line 5. Enter the result as a decimal amount	6
7	Business percentage. For day-care facilities not used exclusively for business, multiply line 6 by line 3 (enter the result as a percentage). All others, enter the amount from line 3	7 20 %
<b>Part II Figure Your Allowable Deduction</b>		
8	Enter the amount from Schedule C, line 29, plus any net gain or (loss) derived from the business use of your home and shown on Schedule D or Form 4797. If more than one place of business, see instructions. See instructions for columns (a) and (b) before completing lines 9-20.	8
	(a) Direct expenses      (b) Indirect expenses	
9	Casualty losses (see instructions)	9
10	Deductible mortgage interest (see instructions)	10 700 00
11	Real estate taxes (see instructions)	11 1,000 00
12	Add lines 9, 10, and 11	12 1,700 00
13	Multiply line 12, column (b) by line 7	13
14	Add line 12, column (a) and line 13	14 340 00
15	Subtract line 14 from line 8. If zero or less, enter -0-	15
16	Excess mortgage interest (see instructions)	16
17	Insurance	17 600 00
18	Repairs and maintenance	18 600 00 100 00
19	Utilities	19 800 00
20	Other expenses (see instructions)	20
21	Add lines 16 through 20	21 600 1,500 00
22	Multiply line 21, column (b) by line 7	22 300 00
23	Carryover of operating expenses from 2001 Form 8829, line 41	23
24	Add line 21 in column (a), line 22, and line 23	24 900 00
25	Allowable operating expenses. Enter the smaller of line 15 or line 24	25
26	Limit on excess casualty losses and depreciation. Subtract line 25 from line 15	26
27	Excess casualty losses (see instructions)	27
28	Depreciation of your home from Part III below	28 140 00
29	Carryover of excess casualty losses and depreciation from 2001 Form 8829, line 42	29
30	Add lines 27 through 29	30 140 00
31	Allowable excess casualty losses and depreciation. Enter the smaller of line 26 or line 30	31
32	Add lines 14, 25, and 31	32
33	Casualty loss portion, if any, from lines 14 and 31. Carry amount to Form 4684, Section B	33
34	Allowable expenses for business use of your home. Subtract line 33 from line 32. Enter here and on Schedule C, line 30. If your home was used for more than one business, see instructions	34
<b>Part III Depreciation of Your Home</b>		
35	Enter the smaller of your home's adjusted basis or its fair market value (see instructions)	35
36	Value of land included on line 35	36
37	Basis of building. Subtract line 36 from line 35	37
38	Business basis of building. Multiply line 37 by line 7	38
39	Depreciation percentage (see instructions)	39 %
40	Depreciation allowable (see instructions). Multiply line 38 by line 39. Enter here and on line 28 above	40
<b>Part IV Carryover of Unallowed Expenses to 2003</b>		
41	Operating expenses. Subtract line 25 from line 24. If less than zero, enter -0-	41
42	Excess casualty losses and depreciation. Subtract line 31 from line 30. If less than zero, enter -0-	42

For Paperwork Reduction Act Notice, see page 4 of separate instructions.

Cat. No. 13232M

Form 8829 (2002)



## Deduction Limit

If your gross income from the business operated or managed from your home equals or exceeds your total business expenses, you can deduct all your business expenses. If your gross income from that use is less than your total business expenses, your deduction for certain expenses for the *business use of your home* is limited.

Gross income is generally the total sales of your business less cost of goods sold.

Your deduction of otherwise nondeductible expenses, such as insurance, utilities and depreciation (with depreciation taken last), is limited to the gross income from the *business use of your home* minus the sum of the following:

- The business part of expenses you could deduct even if you did not use your home for business (such as mortgage interest, real estate taxes and casualty and theft losses).
- The business expenses that relate to the business activity in the home (for example, salaries or supplies), but not to the use of the home itself.

**Example:** Your deduction limit is \$500. Your otherwise nondeductible expenses related to the *business use of the home* are \$800. The deduction for these expenses is limited to \$500.

## Carryforward

Expenses that cannot be deducted because of the deduction limit can be carried forward to later years, subject to the deduction limit in those years.

**Example:** Computing the deduction and carryforward.

Renee has gross income of \$1,500.00 from her private detective agency. She has \$350 in business expenses that do not relate to the *business use of the home*. Her tentative profit is \$1,150 (\$1,500-\$350). Using figures from Exhibit 4.1, the business portion of her expenses are:

Mortgage interest (\$700 x 20%) \$140  
 Real estate taxes (\$1,000 x 20%) 200  
 Direct expenses 600  
 Other indirect expenses 300  
 Depreciation 140

Renee can take a deduction of \$1,150 for expenses related to the *business use of the home*. The remaining \$230 (including all of the depreciation of \$140) is not deductible but can be carried

forward. (See Exhibit 4.2 on page 4-13.)

**EXHIBIT 4.2 – EXPENSES Not RELATED TO BUSINESS USE OF THE HOME, FOR RENEE EXAMPLE**

Form <b>8829</b> Department of the Treasury Internal Revenue Service (99)	<b>Expenses for Business Use of Your Home</b> ▶ File only with Schedule C (Form 1040). Use a separate Form 8829 for each home you used for business during the year. ▶ See separate instructions.	OMB No. 1545-1266 <b>2002</b> Attachment Sequence No. 66																																																																																																																																																																			
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For Paperwork Reduction Act Notice, see page 4 of separate instructions.

Cat. No. 13232M

Form 8829 (2002)



## Where to Deduct Expenses Related to the Business Use of the Home

Self-employed individuals show their business income and expenses on Schedule C (Form 1040), PROFIT OR LOSS FROM BUSINESS, or on Schedule F (Form 1040), PROFIT OR LOSS FROM FARMING. If you file Schedule C, expenses related to the business use of the home are figured on Form 8829, EXPENSES FOR BUSINESS USE OF YOUR HOME and you report the deductible amount on line 30 of Schedule C. If you file Schedule F, figure your deduction using the worksheet at the end of Publication 587, BUSINESS USE OF YOUR HOME, and report the deductible amount on line 34 of Schedule F. Write “*Business Use of Home*” on the dotted line beside the entry.

**Caution:** Do not take a double deduction for real estate taxes and mortgage interest. If you report an amount for the business portion of the taxes and interest on Schedule C (or Schedule F), make sure you report only the personal portion on Schedule A, ITEMIZED DEDUCTIONS. The amounts reported on Schedule C (or F) and Schedule A should be the total interest and taxes you paid for the year.

**Note:** *Employees must itemize deductions on Schedule A (Form 1040) in order to claim the deduction for business use of their home. See Publication 587 for more information.*

## Sale or Exchange of Your Home

If you sell or exchange your home, you may be able to exclude up to \$250,000 (500,000 for certain married persons filing a joint return) of the capital gain on the sale. However, you cannot exclude any part of your gain that is equal to any depreciation allowed or allowable for the *business use of your home* after May 6, 1997. For more information on the sale or exchange of a home, see Publication 523, SELLING YOUR HOME.

### Depreciation

If you used any part of your home for business, you must adjust the basis of your home for any depreciation that was allowable for its business use, even if you did not claim it.

## Recordkeeping

You must keep records that provide the information needed to figure your deductions for the *business use of your home*. You should keep all canceled checks, receipts, invoices and other evidence of expenses you paid.

Your records must show the following information:

- The part of your home you use for business.
- That you use the part of the home exclusively and regularly for business and it is one of the following:
  - your principal place of business or
  - a place where you meet patients, clients or customers in the ordinary course of your business or
  - a separate structure.
- The depreciation and expenses for the business part of your home.

## Exercise

In 2001, Frank started a tax preparation business in his home. He meets the qualifications to deduct *business use of his home*. His house is 2,800 square feet and his office space is 280 square feet. He has the following expenses:

Mortgage interest	\$10,000
Advertising	\$200
Real estate taxes	\$2,500
Home owners insurance	\$500
Office supplies	\$600
Utilities	\$2,200
Paint (for office only)	\$200
General repairs (for home)	\$2,000

The fair market value of the house, which is less than the cost, is \$250,000, and the value of the land is \$40,000. The depreciation percentage is 2.461. His tentative profit on Schedule C is \$30,000.

Compute the *business use of home* deduction for Frank using Form 8829, EXPENSES FOR BUSINESS USE OF YOUR HOME. (See Exhibit 4.3 on page 4-16.)

(Answer on page A-7, Exhibit 4.4 - Filled-in Form 8829.)

EXHIBIT 4.3 - BLANK FORM 8829 FOR EXERCISE

Form <b>8829</b> Department of the Treasury Internal Revenue Service (99)	<b>Expenses for Business Use of Your Home</b> ▶ File only with Schedule C (Form 1040). Use a separate Form 8829 for each home you used for business during the year. ▶ See separate instructions.	OMB No. 1545-1266 <b>2002</b> Attachment Sequence No. 66
Name(s) of proprietor(s)		Your social security number
<b>Part I Part of Your Home Used for Business</b>		
1	Area used regularly and exclusively for business, regularly for day care, or for storage of inventory or product samples (see instructions)	1
2	Total area of home	2
3	Divide line 1 by line 2. Enter the result as a percentage	3 %
• For day-care facilities not used exclusively for business, also complete lines 4-6. • All others, skip lines 4-6 and enter the amount from line 3 on line 7.		
4	Multiply days used for day care during year by hours used per day	4 hr.
5	Total hours available for use during the year (365 days × 24 hours) (see instructions)	5 8,760 hr.
6	Divide line 4 by line 5. Enter the result as a decimal amount	6
7	Business percentage. For day-care facilities not used exclusively for business, multiply line 6 by line 3 (enter the result as a percentage). All others, enter the amount from line 3	7 %
<b>Part II Figure Your Allowable Deduction</b>		
8	Enter the amount from Schedule C, line 29, plus any net gain or (loss) derived from the business use of your home and shown on Schedule D or Form 4797. If more than one place of business, see instructions. See instructions for columns (a) and (b) before completing lines 9-20.	8
		(a) Direct expenses      (b) Indirect expenses
9	Casualty losses (see instructions)	9
10	Deductible mortgage interest (see instructions)	10
11	Real estate taxes (see instructions)	11
12	Add lines 9, 10, and 11	12
13	Multiply line 12, column (b) by line 7	13
14	Add line 12, column (a) and line 13	14
15	Subtract line 14 from line 8. If zero or less, enter -0-	15
16	Excess mortgage interest (see instructions)	16
17	Insurance	17
18	Repairs and maintenance	18
19	Utilities	19
20	Other expenses (see instructions)	20
21	Add lines 16 through 20	21
22	Multiply line 21, column (b) by line 7	22
23	Carryover of operating expenses from 2001 Form 8829, line 41	23
24	Add line 21 in column (a), line 22, and line 23	24
25	Allowable operating expenses. Enter the smaller of line 15 or line 24	25
26	Limit on excess casualty losses and depreciation. Subtract line 25 from line 15	26
27	Excess casualty losses (see instructions)	27
28	Depreciation of your home from Part III below	28
29	Carryover of excess casualty losses and depreciation from 2001 Form 8829, line 42	29
30	Add lines 27 through 29	30
31	Allowable excess casualty losses and depreciation. Enter the smaller of line 26 or line 30	31
32	Add lines 14, 25, and 31	32
33	Casualty loss portion, if any, from lines 14 and 31. Carry amount to Form 4684, Section B	33
34	Allowable expenses for business use of your home. Subtract line 33 from line 32. Enter here and on Schedule C, line 30. If your home was used for more than one business, see instructions	34
<b>Part III Depreciation of Your Home</b>		
35	Enter the smaller of your home's adjusted basis or its fair market value (see instructions)	35
36	Value of land included on line 35	36
37	Basis of building. Subtract line 36 from line 35	37
38	Business basis of building. Multiply line 37 by line 7	38
39	Depreciation percentage (see instructions)	39 %
40	Depreciation allowable (see instructions). Multiply line 38 by line 39. Enter here and on line 28 above	40
<b>Part IV Carryover of Unallowed Expenses to 2003</b>		
41	Operating expenses. Subtract line 25 from line 24. If less than zero, enter -0-	41
42	Excess casualty losses and depreciation. Subtract line 31 from line 30. If less than zero, enter -0-	42
For Paperwork Reduction Act Notice, see page 4 of separate instructions. <span style="float: right;">Cat. No. 13232M      Form 8829 (2002)</span>		

## Lesson 5



# Electronic Filing and Paying Of Business Taxes

## Introduction

If you were one of the more than 46 million taxpayers who filed their personal income tax return using IRS *e-file* in 2002 then you're already aware of the countless benefits electronic filing provides. Now business taxpayers and tax preparers can file by phone, by Internet or by PC software. It's more **E-conomical** with less paperwork. It's more **E-efficient** with increased accuracy. And it's more **E-effective** since you'll spend less time filing tax returns and more time focused on your business. If you're a business taxpayer, ask your tax preparer about *e-filing*. If you're a tax professional, ask your software developer about enabling your programs to take advantage of electronic filing.

This section of the workshop provides an overview of the programs available and a preview of those being developed. You can also obtain additional information online including a listing of Approved IRS *e-file* for Business Providers and Partners – just log on to [www.irs.gov](http://www.irs.gov) and click on the *e-file* logo.

## Objectives

At the end of this lesson, you will be able to:

1. Name the IRS *e-file* for Business programs.
2. Name the benefits of IRS *e-file* for Business programs.
3. Name the Electronic Payment Options.
4. Determine which programs you can use in your business

## References

- **Publication 15**, *Circular E, Employer's Tax Guide*
- **Revenue Procedure 99-39**, *Procedures for the Electronic Filing of Form 941* (contained in Internal Revenue Bulletin 1999-43, dated October 25, 1999), *and*



- **Publication 1855** *Technical Specifications Guide for the Electronic Filing of Form 941, Employer's Quarterly Federal Tax Return (941e-file)*
- Revenue Procedure 2001-9 (released January 16, 2001 as part of **Internal Revenue Bulletin 2001-3**), and, **Publication 3715** *Technical Specifications Guide for the Electronic Filing of Form 940, Employer's Annual Federal Unemployment (FUTA) Tax Return*

## 940 and 941e-file

The IRS electronic employment tax filing program offers business taxpayers a variety of **paperless** options for filing **Form 940** and **Form 941**. Using this program, business taxpayers, reporting agents, software developers and transmitters can file Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, and Form 941, *Employer's Quarterly Federal Tax Return*, electronically. The program conducts security checks, sends electronic acknowledgments and builds records to be processed by IRS computer systems. Returns are transmitted nationwide via dial-up phone lines and menu driven software directly to the IRS where they are processed at the Tennessee Computing Center (TCC)/Memphis Submission Processing Center (MSPC).

**The 941e-file Program** accepts all current quarter tax returns, and returns for four preceding quarters, with the following exceptions:

- Amended Returns
  - Returns with attachments other than Schedule B, (record of federal tax liability).

941e-file and 940e-file returns are signed with a Personal Identification Number (PIN), which is assigned to the Reporting Agent when an application is approved.

A **Form 941** filed through the 941e-file Program has the same due date as a Form 941 filed on paper with due dates as follows:

Quarter Ending	Normal Due Date	Extended Due Date
March 31 <sup>st</sup>	April 30 <sup>th</sup>	May 10 <sup>th</sup>
June 30 <sup>th</sup>	July 31 <sup>st</sup>	August 10 <sup>th</sup>
September 30 <sup>th</sup>	October 31 <sup>st</sup>	November 10 <sup>th</sup>
December 31 <sup>st</sup>	January 31 <sup>st</sup>	February 10 <sup>th</sup>



**Form 940***e-file* returns are annual returns with a calendar year ending and have the same due date as a Form 940 filed on paper – January 31, 2002. If all taxes have been paid in full, the return due date is extended by ten days (February 10, 2002).

**Note:** The extended due dates shown above apply to returns for which all taxes have been paid in full by the normal due date.

### **Who Can Participate in the 940 and 941e-file Programs?**

Business taxpayers using payroll service providers (Reporting Agents) can electronically file Form 941, *Employer's Quarterly Federal Tax Return* and Form 940, *Employer's Federal Unemployment (FUTA) Tax Return* if their service provider offers these services. The payroll service provider electronically transmits your Form 940 and/or 941 return directly to the IRS and beginning in January, 2003, these returns will be processed at the Cincinnati Submission Processing Center (CSPC).

**Note:** In response to customer feedback, the IRS is redesigning the electronic tax filing system for “Employment Taxes”, using a new XML (Extensible Markup Language) file format with expected release in 2003. The new system, referred to as the “Employment Tax *e-file* System” will address user needs by providing a more flexible system and enhanced features, including participation by Electronic Return Originators (EROs). An ERO is a tax professional who has been approved by the IRS to file returns electronically.

If you're a business taxpayer, you'll want to ask your tax preparer about the new Employment Tax *e-file* System. If you're a tax professional, ask your software developer/provider about enabling your tax software program to take advantage of *e-file* for Business.

### **What are the Benefits of 940 and 941e-file?**

#### **It's Convenient**

- It's Paperless! Your PIN serves as your signature.
- Electronic Acknowledgment within 48 hours
- Tax preparation work is automated with return preparation software that performs calculations, and highlights needed forms and schedules

**Fast**

- Information is quickly available to IRS Customer Service sites
- Processing time is reduced to one week or less

**Accurate**

- Fewer risks of transcription errors
- Error rates are less than one percent!

**Safe**

- Tax Information is Secure
- Only authorized users have access to the system

**How to Participate**

Interested participants should have their Reporting Agent submit a completed **Form 9041**, *Application/Registration for Electronic/Magnetic Media Filing of Business Returns*, or a Letter of Application (LOA) to the following address:

Internal Revenue Service  
 AUSPC, Electronic Filing Help Desk  
 Attention: *e-file* Unit, Stop 6380 AUSPC  
 P.O. Box 1231  
 Austin, TX 78767

**Form 9041**, or Letter of Application (LOA) for 941*e-file* must be received by the following dates to be eligible to file a return for the quarter shown:

Application Due Date	For Quarter Ending
December 15 <sup>th</sup>	March 31 <sup>st</sup>
March 15 <sup>th</sup>	June 30 <sup>th</sup>
June 15 <sup>th</sup>	September 30 <sup>th</sup>
September 15 <sup>th</sup>	December 31 <sup>st</sup>

**Application for Form 940e-file**

**Form 9041** or the Letter of Application (LOA) for 940*e-file* must be received by October 15<sup>th</sup> of the year for which the annual FUTA return is due.

Upon IRS approval of the application, a Personal Identification Number (PIN), User-ID/Password/Access Code to access the Electronic Filing System is issued to the participant.

**How can I get more information?**

Visit the [Approved IRS e-file for Business Providers](#) page as well as the [IRS e-file for Business Partners](#) page for a listing of companies that offer IRS *e-file* for Business products and services.

**Tip:** Bookmark these pages as they are updated frequently as new providers and partners are added, and new products and services become available.

## 940/941 On-Line Filing

The IRS On-Line Filing Program for **Form 941** and **Form 940** is available to business filers. The On-Line program, which is a Web-based Internet system, allows business filers to prepare, sign and file Form 941, *Employer's Quarterly Federal Tax Return* and Form 940, *Employer's Annual Federal Unemployment (FUTA) Tax Return*, using an Approved IRS *e-file* for Business Provider also known as a third-party transmitter. Business taxpayers enter their information online by logging on to the approved provider's Web site. The approved provider then transmits the return to the IRS.

### Who can participate in the 940 and 941 On-Line Filing Program?

- Business Filers
- **Approved IRS e-file for Business Providers** also known as third-party transmitters, or software developers

### What are the Benefits?

#### It's Convenient

- It's Paperless! Your PIN serves as your signature
- Electronic Acknowledgment within 48 hours
- Tax preparation work is automated with return preparation software that performs the calculations, and highlights needed forms and schedules

#### Fast

- Information is quickly available to IRS Customer Service sites
- Processing time is reduced to one week or less

#### Accurate

- Fewer risks of transcription errors
- Error rates are less than one percent!

#### Safe

- Tax Information is Secure
- Only authorized users have access to the system

### How to Participate

**Business Filers:** Apply for a Personal Identification Number (PIN) by completing the electronic Letter of Application (LOA) online via the Web, to register through the "Approved IRS *e-file* for Business Provider" (third-party transmitter) of their choice. The third-party transmitter will electronically transmit the LOA to the Austin Submission Processing Center (AUSPC). Upon IRS approval of the business filers' electronic LOA, the IRS mails a Personal Identification Number (PIN) to the business filer within 3 to 5 business days. The business filer uses the PIN to sign their electronic return online. The same PIN is used to sign Forms 940 and 941.

**How can I get more information?**

**Transmitters/Software Developers Only:** Submit a paper **Form 9041**, *Application/Registration for Filing Business Returns* or a paper Letter of Application (LOA) to the Austin Electronic Filing Help Desk to participate in the 941 and/or 940 On-Line Filing Program. Upon IRS approval of the participant's application, the IRS will issue a User-ID/Password/Access Code to access the Electronic Filing System, as applicable.

Help is just a click away at [www.irs.gov](http://www.irs.gov) - click on the *e-file* logo. Remember to visit the **Approved IRS e-file for Business Providers** page as well as the **IRS e-file for Business Partners** page for a listing of companies that offer IRS *e-file* for Business products and services.

If you still have questions, you may contact the following IRS *e-file* Help Desks for assistance. For questions on Form 9041, *Application/Registration for Electronic /Magnetic Media Filing of Business Returns* or Letter of Application (LOA) contact:

Internal Revenue Service  
Austin Submission Processing Center  
Electronic Filing Help Desk  
PO Box 1231  
Austin, TX 78767  
Attn: e-file Unit, Stop 6380 AUSPC  
Telephone: (512) 460-8900 (not toll-free)

Beginning in January 2003, for questions on the 941 e-file Program Contact:

Internal Revenue Service  
Cincinnati Submission Processing Center  
Cincinnati Electronic Filing Help Desk  
201 W. Rivercenter Blvd  
Covington, KY 41012  
Attn: e-file Unit, Stop 2711 CSPC  
Telephone

## 941TeleFile



941TeleFile is an electronic IRS *e-file* option for eligible businesses that choose to electronically file Form 941, *Employer's Quarterly Federal Tax Return*, using a Touch-Tone telephone. It is an interactive computer program that calculates the qualified caller's tax liability or any overpayment and begins the electronic filing process over the phone. This program is paperless (no forms are required to be mailed) and it's FREE.

941TeleFile users can elect to electronically file and simultaneously pay any balance due on the return by using Electronic Funds Withdrawal, formerly known as Direct Debit (automatic withdrawal).

### Who can participate in 941TeleFile?

Businesses that receive the special 941TeleFile Tax Record and Instructions as part of their Form 941 Tax Package must meet the qualifications in the instructions.

#### Your Can use 941 TeleFile if you:

- Receive the special TeleFile Tax Record as part of your 941 package;
- Are a monthly schedule depositor for the entire quarter;
- Have not changed your business name, address or Employer Identification Number (EIN) during the previous quarter;
- Must have a break-even, overpayment (to be applied to the next quarter), or balance due return (using electronic funds withdrawal);
- Are not a seasonal employer;
- Have no schedules or attachments (if you are required to file a Schedule B you are not eligible to use 941TeleFile);
- Only have fractions of cents adjustments; and
- Choose to claim Advance Earned Income Credit (AEIC) payments. (Optional)

**NEW !**

Beginning April 1, 2002, there's an even faster and easier way to file Form 941. Certain business taxpayers are eligible to file the new **941TeleFile "Zero Wage Return"**. You must have no employees, no withholding, no deposits and no taxes to report to be eligible.

**What are the Benefits of 941TeleFile?**

- **It's Convenient** - 941TeleFile is easy to use and provides step-by-step instructions over the phone. The 941TeleFile Tax Record is an official record of your tax return. You also receive proof of filing - when you have finished the call and the IRS has accepted your return, the 941TeleFile system provides you with a confirmation number. You can even choose to electronically pay any balance due by authorizing an Electronic Funds Withdrawal from your bank account.
- **It's Fast** – Information is quickly available to IRS Customer Service sites and processing time is greatly reduced.
- **It's Accurate** – It does the math - 941TeleFile computes your tax liability and any overpayment or balance due during the call. All entries are repeated to double-check accuracy.
- **It's Safe** – Tax information is secure. Only authorized users have access to the system.

**How to Participate**

Businesses that receive the special tax package must complete the 941TeleFile Tax Record before using a touch-tone telephone to place their call using the special toll-free number listed in the 941TeleFile tax package. The interactive program prompts users to make the necessary entries from the TeleFile Tax Record, using the telephone keypad. The system repeats each entry to verify accuracy and to allow users to immediately correct any mistakes.

Next, the system provides the overpayment or balance due amount to be entered on the TeleFile Tax Record that should be retained by the filer. The system then plays a jurat statement and asks the caller to enter his or her identification information, which constitutes the electronic signature. (Refer to 941TeleFile Instructions) The electronic signature should be for the authorized signer (member, officer or agent of the taxpayer), followed by the

pound (#) sign. This alternative signature method makes the 941TeleFile option completely paperless.

Last, a ten-digit confirmation number is issued to the caller as proof of filing. If the caller did not hear the confirmation number or misplaces it, he/she may call the toll-free number again. The system will ask for the caller's Employer Identification Number (EIN). Once the EIN is entered, the ten-digit proof of filing confirmation number is repeated.

If the system will not accept the information being entered, determine if the correct telephone keypad buttons are being used to make entries. For instance, do not use the letter "O" for a number zero (0) or the letter "L" for number one (1).

If an error is made but not realized until after hanging up, the caller must file a corrected paper return.

### **Payment Options for 941Tele-File**

- It's free and convenient - You can electronically file and pay all at once.
- It's safe and secure - Electronic Funds Withdrawal information will be used only for the tax payment you authorize. No other withdrawals can legally be made.
- Bank account information is safeguarded with other tax information.
- Payment information will not be disclosed for any reason other than processing the transaction as authorized.
- The tax payment is included on the monthly bank statement, as a *United States Treasury Tax Payment*, as proof of payment.
- You will be prompted by the 941TeleFile script to enter bank account information.
- You must know the account number and financial institution's Routing Transit Number (RTN).
- You must identify the type of account from which the payment is to be made (checking or savings).
- Account numbers and Routing Transit Numbers can be found on checks and share drafts.

- Check with your financial institution if you have questions regarding these numbers and to confirm that the financial institution will allow an Electronic Funds Withdrawal from the account.

### **If you choose to pay using Electronic Funds Withdrawal**

- You may authorize the U.S. Department of the Treasury (through a Treasury Financial Agent) to transfer money from your bank account to the Treasury account.
  - The payment date will be the same as the date the balance due return is filed.
  - Electronic Funds Withdrawal payments will be withdrawn in a single transaction, not installments.
  - You can call the Treasury Financial Agent, toll-free at 1-888-353-4537 to inquire about payments. Wait at least 5 days after the return is filed before making inquiries.
  - You will be notified if a payment is returned by the financial institution due to insufficient funds, incorrect account information, closed accounts, etc. If this occurs, the IRS will send a notification letter to the address on the tax return explaining why the payment could not be processed. The letter will include instructions for sending a check to a unique address that has been established for this initiative.
  - In the event the financial institution is unable to process the direct debit transaction, you will be responsible for the tax payment in addition to penalties and interest.
  - Contact the IRS immediately at 1-800-829-1040 if there is an error in the amount withdrawn.
  - In the event Treasury causes an incorrect amount of funds to be withdrawn from the bank account, Treasury is responsible for returning any improperly transferred funds.

### **1065 e-file for Partnerships**

Partnerships that engage in a trade or business or have gross income from sources within the United States may be able to electronically file Form 1065, *U.S. Partnership Return of Income*.



**Legislative  
Mandate**

Effective December 31, 2000, partnerships with more than 100 partners are now *required* to file their Form 1065, Schedules K-1 and related forms and schedules electronically. Failure to comply with the provisions of the mandate could result in an assessment of a penalty.

The electronic filing mandate applies only to those partnerships with more than one hundred partners, however businesses may choose to *voluntarily* electronically file their Forms 1065 regardless of the number of partners in the partnership.

Certain partnership filers are *excluded from the mandate* as shown below.

- Form 1065-B Returns
- Form 1065 with a foreign address
- Amended Returns
- Returns filed under Sections 6020(b), 501(d)(3) or 761(a) of the Internal Revenue Code
- Fiscal Year Partnership Returns
- Fiscal Year Short Period Returns
- Fiscal Year Final Returns

**Benefits of 1065 e-file**

- Less paper handling
- Reduced costs
- Improved accuracy and product quality (fewer errors mean less correspondence with the IRS)
- Electronic acknowledgment of return

A complete listing of Approved IRS *e-file* for Business Providers who offer 1065 *e-file* can be found at [www.irs.gov](http://www.irs.gov) - click on the *e-file* logo. Links to these companies' Web sites are included.

**TIP: You may be able to enter your return information online via the Internet using software provided by the 1065 *e-file* provider of your choice. The provider will then transmit your Form 1065 and K-1s to the IRS.**

**Note: If you've chosen to use the services of an Approved IRS *e-file* for Business Provider to electronically file your Form 1065, you do *not* need to submit an application.**

All others must submit Form 9041, *Application/Registration for Electronic/Magnetic Media Filing of Business Returns*, to the IRS Austin Submission Processing Center (AUSPC) in Austin, Texas for processing. The IRS accepts applications by mail or fax.

Internal Revenue Service  
Austin Submission Processing Center  
ATTN: EFU, Stop 6380  
P.O. Box 1231  
+Austin, TX 78767  
Fax: (512) 460-8962 (not toll-free)

## Products In Development



### 1120/1120S *e-file* Program

Beginning January 2004, corporations will be able to electronically file Form 1120, *U.S. Corporation Income Tax Return* and Form 1120S, *U.S. Income Tax Return for an S Corporation* as well as 53 associated forms and schedules. A Fed/State electronic filing option is planned for 2005.

With EFTPS, you can make your federal tax payments electronically instead of using paper deposit coupons. There are no more last minute trips to the bank, lost checks, inaccurate forms or postage costs. EFTPS is a **free** payment system sponsored by the U.S. Department of the Treasury.

#### The EFTPS System

- **Currently serves more than 4 million business taxpayers**
- **Enrolls 6,500 new businesses each week**
- **Is available to all business taxpayers**

**Note:** Only businesses that make in excess of \$200,000 in total yearly deposits are required to enroll in EFTPS, however it is available for use by all taxpayers.

EFTPS offers you the convenience of making your federal tax payment directly by EFTPS-Phone (voice response system), EFTPS-PC Software (personal computer), EFTPS-OnLine (Internet) or EFTPS-through a Financial Institution. You can initiate your tax payment **24 hours a day, 7 days a week**. EFTPS even allows businesses to schedule their tax payment instructions up to 120 days in advance of the date you designate. No special equipment is required to use EFTPS; and, if you use a PC, free Windows®-based software is available. Whether you use a phone, PC, Internet or a service offered by a financial institution, you are in charge of initiating your tax payments through EFTPS. No one has unauthorized access to your account. You will also receive an Electronic Funds Transfer (EFT) Acknowledgment Number to keep as a record of your payment.

## Pay Your Taxes Electronically

You can use EFTPS to pay these taxes:

FORM 720 QUARTERLY FEDERAL EXCISE RETURN  
 FORM 940 EMPLOYER’S ANNUAL FEDERAL UNEMPLOYMENT TAX (FUTA) RETURN  
 FORM 941 EMPLOYER’S QUARTERLY FEDERAL TAX RETURN  
 FORM 943 EMPLOYER’S ANNUAL TAX RETURN FOR AGRICULTURE WORKERS  
 FORM 945 ANNUAL RETURN OF WITHHELD FEDERAL INCOME TAX  
 FORM 990-C FARMER’S COOPERATIVE ASSOCIATION INCOME TAX RETURN  
 FORM 990-PF RETURN OF PRIVATE FOUNDATION  
 FORM 990-T EXEMPT ORGANIZATION BUSINESS INCOME TAX RETURN  
 SECTION 4947 (A)(1) CHARITABLE TRUST TREATED AS A PRIVATE FOUNDATION  
 FORM 1041 FIDUCIARY INCOME TAX RETURN  
 FORM 1042 ANNUAL WITHHOLDING TAX RETURN FOR U.S. SOURCES OF INCOME OF FOREIGN PERSONS  
 FORM 1120 U.S. CORPORATION INCOME TAX RETURN  
 FORM CT-1 EMPLOYER’S ANNUAL RAILROAD RETIREMENT TAX RETURN

*In addition, you can use EFTPS to make all your federal tax payments, including income, employment, estimated, excise and installment agreement payments.*

## Payment Options

On Form 9779, EFTPS BUSINESS ENROLLMENT FORM, you will be asked to select from the following primary payment methods are:

- **EFTPS–Direct**
- **EFTPS–Through a Financial Institution**

You also have the option to use a **Same Day Payment** method, although many financial institutions charge significant fees for using this method.

### **EFTPS–Direct (Automated Clearinghouse (ACH) Debit)**

If you select this method of payment, you will receive a Personal Identification Number (PIN). Your PIN must be used in combination with your Taxpayer Identification Number (TIN) to gain access to EFTPS. EFTPS will move the funds from your account to the Treasury’s account on the date you designate. **Funds will not move from your account until the date you indicate.**

**Step 1.** At least one calendar day before your tax due date, and before 8:00 p.m. ET, you access EFTPS by phone or PC. EFTPS will then prompt you for the necessary information to complete your tax payment report.

**Step 2.** The system processes the information reported.

When the information is accepted, you will receive an EFT Acknowledgment Number. Keep this number for your records in case of questions at a later date.

**Step 3.** Once your tax payment report is accepted, EFTPS will originate an ACH Debit transaction against your designated account on the date you indicated when making your payment.

**Step 4.** The funds will be transferred to the Treasury's account and the tax data will be reported to IRS to update your tax records.

### **EFTPS–Through a Financial Institution (ACH Credit)**

In this method, you will instruct your financial institution to electronically move funds from your account to the Treasury's Account. However, not all financial institutions offer this service. Therefore, before selecting this option, you should first check with your bank to see if they offer this service, how much it costs, and if you are eligible to use it.

**Step 1.** At least one day before the tax due date, you initiate your payment through your financial institution. The tax payment report must be made prior to your financial institution's ACH processing deadline.

**Step 2.** Your financial institution will originate an ACH Credit transaction to EFTPS, transferring the funds to the Treasury's Account and the tax data to IRS to update your tax records.

### **Same Day Payment**

**While EFTPS-Direct and EFTPS-Through a Financial Institution** are the primary payment methods for EFTPS, you can also use the **Same Day Payment** method. Check with your financial institution for fees involved. Typically, the cost of Same Day Payments is higher than the other payment methods.

### **Payroll Company**

If you choose to allow your payroll company to make tax payments on your behalf, you should check with them for specific fees, deadlines and instructions pertaining to enrollment in EFTPS.



**If your payroll company is not making all of your tax payments through EFTPS, you will need to enroll in EFTPS to initiate those payments not processed by them. It is also a good idea to enroll in EFTPS separately so that you have flexibility if you ever need to change payroll companies.**

### **Scheduling Feature**

As a bonus, if you are out of town when your tax payment is due,

or you want to plan ahead, EFTPS offers a Payment Scheduling feature. Businesses may schedule payment instructions up to 120 days in advance of the tax due date; individuals may schedule payment instructions up to 365 days in advance of tax the due date and EFTPS will automatically make the payments on the due date indicated.

## **New Banking Feature**

It is now easier for taxpayers to pay taxes electronically to change their banking information. Taxpayers can now make changes to their financial institution information over the phone. Using **EFTPS-Phone**, taxpayers call the 1-800 number for an automated way to add new financial institution account information. If the taxpayer elects not to have their financial information verified by their bank, they will receive a new Personal Identification Number (PIN) immediately over the phone and can continue using EFTPS. If users choose to have their information verified, an additional 7-10 days is required for processing, after which time taxpayers will receive a new PIN in the mail. EFTPS users can also use **EFTPS-OnLine** to make changes and receive a new PIN within 7-10 days by U.S. Mail.

## **Customer Service and Enrollment**

Once you enroll in EFTPS, you will have dedicated Customer Service Representatives to answer any questions about your payments. Customer Service Centers are open 24 hours a day, 7 days a week. For more information or to enroll call **1-800-555-4477** or **1-800-945-8400** or visit **www.eftps.gov**.

## **After Enrollment**

Once you have completed and mailed your enrollment form, EFTPS processes your enrollment and sends you a confirmation package, including a step-by-step Payment Instruction Booklet (PIB). Your PIN will be sent under separate cover. Once you receive your PIN, you can begin making payments.

**IMPORTANT!** If your Enrollment Form is incomplete and cannot be processed, you will receive notification from EFTPS regarding any missing information.

## **References**

- Publication 966, EFTPS – *NOW A FULL RANGE OF ELECTRONIC CHOICES TO PAY ALL YOUR FEDERAL TAXES*
- Publication 3425- *5 Easy Ways to Use EFTPS, for Tax Practitioners, Accountants and Payroll Companies*
- Publication 3959, EFTPS CD-ROM for Taxpayers (Business and Individuals)
- Form 9779, *EFTPS BUSINESS ENROLLMENT FORM*

Exhibit – Form 9779, Page 1



**Tax Form 9779 with Instructions** (OMB 1545-1467)



**Business Enrollment Form for EFTPS** – This form contains instructions to complete the Electronic Federal Tax Payment System (EFTPS) Enrollment Form for Business Taxpayers. It is to be used either for initial enrollment in the system or to add financial institution information. If you wish to use multiple accounts in one financial institution, or accounts in multiple financial institutions, you will need to provide multiple copies of the enrollment form.

For questions regarding EFTPS or this Enrollment Form please call: **EFTPS Customer Service** 1-800-555-4477 or 1-800-945-8400  
 Visit our web site at [www.EFTPS.gov](http://www.EFTPS.gov) to enroll online. For TDD (hearing impaired) support 1-800-733-4829 or 1-800-945-8900  
 24 hours a day, 7 days a week en español 1-800-244-4829 or 1-800-945-8600

➔ When your form is completed, please mail to: **EFTPS Enrollment Processing Center**  
**P.O. Box 4210**  
**Iowa City, Iowa 52244-4210**

You should receive your Confirmation/Update Form and instructions on using EFTPS approximately two to four weeks after we receive your Enrollment Form.

**INSTRUCTIONS**

- Employer Identification Number (EIN).** Enter your nine-digit Employer Identification Number. Enter the EIN on the back of the form in the upper right corner as well.
- Business Taxpayer Name.** Print your business name exactly as it appears on the tax return. The only valid characters are A-Z, 0-9, -, &, and blank.
- Business Address.** This address should be the address as it appears on the business tax return.

**Note:** If the address has been pre-printed and is incorrect, it can only be changed by submitting an IRS Change of Address (Form 8822) to the Internal Revenue Service. The address on your EFTPS enrollment will automatically be updated when Form 8822 is submitted. See the back of Form 8822 to determine where the form should be mailed.

- Marking Instructions:
- Use black or blue ink only.
  - Please print legibly. Use one character per block. Use only capital letters. Keep all printing within the boxes.
  - Do not make any stray marks on this form.

MARKING EXAMPLE:

IA	52471
State	Zip Code

**Taxpayer Information**

1. Employer Identification Number (EIN) – (Please enter EIN on reverse side also.)

2. Business Taxpayer Name:

3. Business Street Address:

City:  State:  ZIP Code:

International: Province, Country, and Postal Code:

**Contact Information**

4. Primary Contact Name:

5. Primary Contact Mailing Street Address (if different from #3 above):

City:  State:  Zip Code:

International: Province, Country, and Postal Code:

6. Primary Contact Phone Number:  
 US Area Code    International 011- Country Code  City Code

7. Primary Contact E-mail Address (use as many spaces as needed up to 60):

- Primary Contact Name.** Print the name of a person, company, or third party who can be contacted in the event questions arise regarding this enrollment or tax payments. All EFTPS mailings will be sent to your primary contact.
- Primary Contact Mailing Address and Phone Number (if different from #3 above).** You need not complete the address area if your contact's address is the same as the business address. If an address is provided here, it will be used to mail confirmation materials and instruction booklets.
- Primary contact E-mail Address.** (optional)

EXHIBIT - Form 9779, Page 2



(continued)

For side 2 please fill in

Employer Identification Number (EIN)

EIN:

**Payment Information**

**8. Payment Method.** Choose the payment method(s) by placing an "X" in the box(es). The options available are: EFTPS-Direct and EFTPS-Through A Financial Institution.

When choosing EFTPS-Direct you can use EFTPS-Phone, EFTPS-OnLine or EFTPS-PC Software. \*If you choose EFTPS-PC Software, and after your EFTPS enrollment is successful, you may download the software from our web site ([www.EFTPS.gov](http://www.EFTPS.gov)), or to receive the software via mail, call EFTPS Customer Service at the numbers listed on the front of this form.

8. Payment Method

**EFTPS-Direct:** check here if you will instruct EFTPS to transfer payment from your account. (These EFTPS Payment Input Methods for EFTPS-Direct are interchangeable: EFTPS-Phone, EFTPS-PC Software \*, EFTPS-OnLine)

**EFTPS-Through A Financial Institution:** check here if you will instruct your financial institution to forward the payment to EFTPS. You must check with your financial institution to determine if they are capable of providing this service.

**NOTE: If you will only be using EFTPS-Through A Financial Institution as a payment method, skip to item #23.**

**Note:** For EFTPS-Direct, complete the additional information required about your financial institution. Enrollment in the EFTPS-Direct payment method will automatically enroll you for EFTPS-Through A Financial Institution as well as Same-Day Payment.

For EFTPS-Through A Financial Institution, you initiate a tax payment through a financial institution. You must contact your financial institution to insure the institution is capable of making an EFTPS payment through the Automated Clearing House (ACH) or a Same-Day Payment method. If you enroll for EFTPS-Through A Financial Institution or Same-Day Payment, you may also enroll for EFTPS-Direct by providing the financial institution information requested on items 19 through 23.

**9-18. Optional Tax Form Payment Amount Limits (For EFTPS-Direct only)**

This section is optional. You may set amount limits for each tax type to prevent an overpayment. The system will compare your payment amount against your stated limit and provide a warning if you exceed the limit. You may override the warning if you wish.

(19 through 24 must be completed if EFTPS-Direct will be used)

**19. RTN.** This is the nine-digit number associated with your financial institution. You may contact your financial institution to verify this number.

**20. Account Number.** Enter the number of the account you will use to pay your taxes.

**21. Type.** Please mark one box to indicate whether the account is a checking or savings account.

**22. State and ZIP Code.** Use the two-character letter abbreviation for the state your financial institution is located in and indicate ZIP Code.

**23. Authorization.** This section authorizes a Financial Agent of the U.S. Treasury to initiate tax payments from the account(s) you designate if you requested the EFTPS-Direct payment method.

**24. Taxpayer Signature.** The taxpayer must sign this section to authorize participation in EFTPS. If there is no signature, a form will be returned.

This section also provides authorization to share the information provided with your financial institution, required for the processing of the Electronic Federal Tax Payment System.

If signed by a corporate officer, partner, or fiduciary on behalf of the taxpayer, the signer certifies that they have the authority to execute this authorization on behalf of the taxpayer.

**Remember to sign and mail your enrollment form to the address on reverse side.**

**Tax Form Payment Amount Limits** (EFTPS-Direct only)

9. 720	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	10. 940	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	11. 941	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
12. 943	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	13. 945	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	14. 990C	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
15. 990PF	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	16. 990T	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	17. 1042	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
18. 1120	\$	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>												

**Financial Institution Information** (to be completed if EFTPS-Direct will be used)

19. RTN:

20. Account Number:

21. Type:  Checking  Savings

22. State:

ZIP Code:

**Authorization**

23. For both payment methods: Please read the following Authorization Agreement:

I (as defined as the taxpayer whose signature is below) hereby authorize the contact person (listed in item #4 of this form) and the financial institutions involved in the processing of my Electronic Federal Tax Payment System (EFTPS) payments to receive confidential information necessary to effect enrollment in EFTPS, electronic payment of taxes, and answer inquiries and resolve issues related to enrollment and payments. This information includes, but is not limited to, passwords, payment instructions, taxpayer name and identifying number, and payment transaction details. If signed by a corporate officer, partner, or fiduciary on behalf of the taxpayer, I certify that I have the authority to execute this authorization on behalf of the taxpayer. This authorization is to remain in full force and effect until the designated Financial Agents of the U.S. Treasury have received notification from me of termination in such time and in such manner to afford a reasonable opportunity to act on it.

Only EFTPS-Direct: Please read the following Authorization Agreement:

By completing the information in boxes 19-22 and signing below, I hereby authorize designated Financial Agents of the U.S. Treasury to initiate EFTPS-Direct debit entries to the financial institution account indicated above, for payment of Federal taxes owed to the IRS upon request by taxpayer or his/her representative, using the Electronic Federal Tax Payment System (EFTPS). I further authorize the financial institution named above to debit such entries to the financial institution account indicated above. All debits initiated by the U.S. Treasury designated Financial Agents pursuant to this authorization shall be made under U.S. Treasury regulations. This authorization is to remain in full force and effect until the designated Financial Agents of the U.S. Treasury have received written notification from me of termination in such time and in such manner as to afford a reasonable opportunity to act on it.

24. Taxpayer Signature

\_\_\_\_\_  
Taxpayer Signature

\_\_\_\_\_  
Date

\_\_\_\_\_  
Print Name

\_\_\_\_\_  
Title

Paperwork Reduction Act Notice: In accordance with the Paperwork Reduction Act of 1995, we ask for the information in the Electronic Federal Tax Payment System (EFTPS) Enrollment Form in order to carry out the requirements of 28 United States Code 6001, 6011, and 6109. You are not required to provide information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Code section 6103. This information is used by the Internal Revenue Service to assure that payment(s) are properly credited to the appropriate account(s). Your response is mandatory if you are required by regulations to use Electronic Funds Transfer to make your Federal Tax Deposits. The time needed to provide this information will vary depending on individual circumstances. The estimated average time is ten minutes. If you have comments concerning the accuracy of this time estimate or suggestions for reducing this burden, we would be happy to hear from you. You can write to the Internal Revenue Service, Tax Forms Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. Please do not send the enrollment form to this address.

The Privacy Act of 1974 requires that when we ask individuals for information about themselves, we state our legal right to ask for the information, why we are asking for the information, and how it will be used. We must also tell you what could happen if we do not receive all or part of it, and whether your response is voluntary, required to obtain a benefit, or mandatory. Our legal right to ask for information is 5 U.S.C. 301 and Internal Revenue Code sections 6001, 6011, 6012, and applicable regulations. The information will be used to enroll you in the Electronic Federal Tax Payment System (EFTPS). The information may not be disclosed except as provided by section 6103 of the Internal Revenue Code. We may give the information to the Department of Justice and to other Federal agencies, as provided by law. We may also give it to cities, states, the District of Columbia, and U.S. commonwealths or possessions to carry out their laws. We may give it to foreign governments because of tax treaties they have with the United States. Your response is mandatory if you are required by regulations to use electronic funds transfer to make your deposits. If you are not required by regulations to use electronic funds transfer, your response is voluntary. If you do not provide all or part of the information, you may not be eligible to participate in the EFTPS. If you are required to use electronic funds transfer by regulation, you may be subject to penalties. If you are not required to use electronic funds transfer to pay taxes owed, you need to pay the taxes due by another method.



Form 9779 (Rev. 7-2002)  
Catalog Number 21816U

# Answers

## Lesson 2

### Exercise 1

1. Form SS-4, APPLICATION FOR EMPLOYER IDENTIFICATION NUMBER.
2. Form W-4.
3. (A1) 6.2% social security tax rate and  
(A2) 1.45% Medicare tax rate  
(B) Same as above  
(C) \$84,900 wage base limit in 2002 for social security tax  
(D) No wage base limit for Medicare tax
4. (A) Form W-2  
(B) By January 31 of the following year
5. Form 1099-MISC
6. 30%
7. Form W-5
8. Forms W-2c and W-3c



## Lesson 3, Part 1

### Exercise 1

Deposit Date	Amount
5/15/02	\$1,343.82
6/17/02	2,491.56
7/16/02	2,241.62
Total	<u>\$ 6,077.00</u>

See filled-in Exhibit 3.8 page A-3.

### Exercise 2

Social Security Tax	\$ <u>0</u>
Medicare Tax	<u>0</u>
Federal Income Tax	\$ <u>8</u>

### Exercise 3

Deposit Date by	Amount	Monthly Amount
Wednesday 10/9/02	\$10,528.82	
Wednesday 10/23/02	10,253.20	\$20,782.02
Wednesday 11/6/02	9,514.50	
Wednesday 11/20/02	9,975.28	\$28,913.52
Wednesday 12/4/02	9,423.74	
Wednesday 12/18/02	10,528.82	
Thursday 1/2/03	10,528.82	
Thursday 1/2/03	764.00	\$21,821.64
Total	\$71,517.18	\$71,517.18

See filled-in Exhibit 3.9 pages A-4 and A-5.

ANSWER TO EXERCISE 1 – EXHIBIT 3.8

**Form 941**  
(Rev. January 2002)  
Department of the Treasury  
Internal Revenue Service (99)

**Employer's Quarterly Federal Tax Return**

▶ See separate instructions revised January 2002 for information on completing this return.

Please type or print.

OMB No. 1545-0029

T
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Enter state code for state in which deposits were made **only** if different from state in address to the right ▶

Name (as distinguished from trade name) **Green For Ever, Inc.**

Trade name, if any

Address (number and street) **925 Fern Ave.**

Date quarter ended **6/30/2002**

Employer identification number **10-1234567**

City, state, and ZIP code **Augusta, GA 32599**

If address is different from prior return, check here ▶

1	1	1	1	1	1	1	1	2	3	3	3	3	3	3	4	4	4	5	5	5	
6	7	8	8	8	8	8	8	8	9	9	9	9	9	9	10	10	10	10	10	10	10

If you do not have to file returns in the future, check here ▶  and enter date final wages paid ▶

If you are a seasonal employer, see **Seasonal employers** on page 1 of the instructions and check here ▶

1 Number of employees in the pay period that includes March 12th . . . ▶	1		
2 Total wages and tips, plus other compensation . . . . .	2	26830	00
3 Total income tax withheld from wages, tips, and sick pay . . . . .	3	1972	00
4 Adjustment of withheld income tax for preceding quarters of calendar year . . . . .	4		
5 Adjusted total of income tax withheld (line 3 as adjusted by line 4—see instructions) . . . . .	5	1972	00
6 Taxable social security wages . . . . .	6a	26830	00
	6b	$\times 12.4\% (.124) =$	
6 Taxable social security tips . . . . .	6c		
	6d	$\times 12.4\% (.124) =$	
7 Taxable Medicare wages and tips . . . . .	7a	26830	00
	7b	$\times 2.9\% (.029) =$	
8 Total social security and Medicare taxes (add lines 6b, 6d, and 7b). Check here if wages are not subject to social security and/or Medicare tax . . . . .	8	4104	99
9 Adjustment of social security and Medicare taxes (see instructions for required explanation) Sick Pay \$ ± Fractions of Cents \$ <b>+01</b> ± Other \$ =	9		01
10 Adjusted total of social security and Medicare taxes (line 8 as adjusted by line 9—see instructions) . . . . .	10	4105	00
11 Total taxes (add lines 5 and 10) . . . . .	11	6077	00
12 Advance earned income credit (EIC) payments made to employees . . . . .	12		
13 Net taxes (subtract line 12 from line 11). <b>If \$2,500 or more, this must equal line 17, column (d) below (or line D of Schedule B (Form 941))</b> . . . . .	13	6077	00
14 Total deposits for quarter, including overpayment applied from a prior quarter . . . . .	14	6077	00
15 Balance due (subtract line 14 from line 13). See instructions . . . . .	15		

16 Overpayment. If line 14 is more than line 13, enter excess here ▶ \$

and check if to be:  Applied to next return or  Refunded.

- All filers: If line 13 is less than \$2,500, you need not complete line 17 or Schedule B (Form 941).
- Semiweekly schedule depositors: Complete Schedule B (Form 941) and check here . . . . . ▶
- Monthly schedule depositors: Complete line 17, columns (a) through (d), and check here. . . . . ▶

17 Monthly Summary of Federal Tax Liability. Do not complete if you were a semiweekly schedule depositor.			
(a) First month liability	(b) Second month liability	(c) Third month liability	(d) Total liability for quarter
1343.82	2491.56	2241.62	6077.00

Third Party Designee: Do you want to allow another person to discuss this return with the IRS (see separate instructions)?  Yes. Complete the following.  No

Designee's name ▶ Phone no. ▶ ( ) Personal identification number (PIN) ▶

Sign Here: Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. **R.M. Green, Jr. Treas.**

Signature = *R. M. Green Jr.* Print Your Name and Title = Date =

For Privacy Act and Paperwork Reduction Act Notice, see back of Payment Voucher. Cat. No. 17001Z Form 941 (Rev. 1-2002)

ANSWER TO EXERCISE 3 – EXHIBIT 3.9

**Form 941**  
(Rev. January 2002)  
Department of the Treasury  
Internal Revenue Service (99)

**Employer's Quarterly Federal Tax Return**

▶ See separate instructions revised January 2002 for information on completing this return.  
Please type or print.

OMB No. 1545-0029

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Enter state code for state in which deposits were made **only** if different from state in address to right (see page 2 of instructions).

Name (as distinguished from trade name) **Paul's Auto Shop, Inc.**  
Trade name, if any

Address (number and street) **425 Auto Strip Drive**

Date quarter ended **12/31/2002**  
Employer identification number **10-9876543**  
City, state, and ZIP code **Cando, LA 88877**

If address is different from prior return, check here

IRS Use

1	1	1	1	1	1	1	1	1	1	2	3	3	3	3	3	3	4	4	4	5	5	5	
6	7	8	8	8	8	8	8	8	8	8	9	9	9	9	9	9	9	10	10	10	10	10	10

If you do not have to file returns in the future, check here  and enter date final wages paid ▶

If you are a seasonal employer, see **Seasonal employers** on page 1 of the instructions and check here ▶

1 Number of employees in the pay period that includes March 12th . . . ▶	1	
--	---	--

2 Total wages and tips, plus other compensation . . . . .	2	206460 00
3 Total income tax withheld from wages, tips, and sick pay . . . . .	3	40165 00
4 Adjustment of withheld income tax for preceding quarters of calendar year . . . . .	4	
5 Adjusted total of income tax withheld (line 3 as adjusted by line 4—see instructions) . . . . .	5	40165 00
6 Taxable social security wages . . . . .	6a	206460 00 × 12.4% (.124) =
Taxable social security tips . . . . .	6c	× 12.4% (.124) =
7 Taxable Medicare wages and tips . . . . .	7a	206460 00 × 2.9% (.029) =
8 Total social security and Medicare taxes (add lines 6b, 6d, and 7b). Check here if wages are not subject to social security and/or Medicare tax . . . . .	8	31588 38
9 Adjustment of social security and Medicare taxes (see instructions for required explanation) Sick Pay \$ _____ ± Fractions of Cents \$ <b>-20</b> ± Other \$ _____ =	9	(20)
10 Adjusted total of social security and Medicare taxes (line 8 as adjusted by line 9—see instructions) . . . . .	10	31588 18
11 Total taxes (add lines 5 and 10) . . . . .	11	71753 18
12 Advance earned income credit (EIC) payments made to employees . . . . .	12	236 00
13 Net taxes (subtract line 12 from line 11). <b>If \$2,500 or more, this must equal line 17, column (d) below (or line D of Schedule B (Form 941))</b> . . . . .	13	71517 18
14 Total deposits for quarter, including overpayment applied from a prior quarter . . . . .	14	71517 18
15 Balance due (subtract line 14 from line 13). See instructions . . . . .	15	

16 Overpayment. If line 14 is more than line 13, enter excess here ▶ \$ \_\_\_\_\_ and check if to be:  Applied to next return or  Refunded.

- All filers: If line 13 is less than \$2,500, you need not complete line 17 or Schedule B (Form 941).
- Semiweekly schedule depositors: Complete Schedule B (Form 941) and check here . . . . .
- Monthly schedule depositors: Complete line 17, columns (a) through (d), and check here. . . . .

17 Monthly Summary of Federal Tax Liability. Do not complete if you were a semiweekly schedule depositor.			
(a) First month liability	(b) Second month liability	(c) Third month liability	(d) Total liability for quarter

Third Party Designee: Do you want to allow another person to discuss this return with the IRS (see separate instructions)?  Yes. Complete the following.  No

Designee's name ▶ \_\_\_\_\_ Phone no. ▶ ( ) \_\_\_\_\_ Personal identification number (PIN) ▶ \_\_\_\_\_

Signature Here: Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. **Paul Potter, Pres.**

Signature = *Paul Potter* Print Your Name and Title = \_\_\_\_\_ Date = \_\_\_\_\_

For Privacy Act and Paperwork Reduction Act Notice, see back of Payment Voucher. Cat. No. 170012 Form 941 (Rev. 1-2002)

ANSWER TO EXERCISE 3 – EXHIBIT 3.9

<p><b>SCHEDULE B (FORM 941)</b> (Rev. January 2002) Department of the Treasury Internal Revenue Service</p>	<p><b>Employer's Record of Federal Tax Liability</b> ▶ See Circular E for more information about employment tax returns. <b>5151</b> ▶ Attach to Form 941 or 941-SS.</p>	<p>OMB No. 1545-0029</p>			
<p>Name as shown on Form 941 (or Form 941-SS) <b>Paul's Auto Shop, Inc.</b></p>		<p>Employer identification number <b>10 : 9876543</b></p>			
		<p>Date quarter ended <b>12/31/2002</b></p>			
<p>You must complete this schedule if you are required to deposit on a semiweekly schedule, or if your tax liability on any day is \$100,000 or more. Show tax liability here, <b>not</b> deposits. (The IRS gets deposit data from FTD coupons or EFTPS.)</p>					
<b>A. Daily Tax Liability—First Month of Quarter</b>					
1	8	15	22	29	
2	9	16	23	30	
3	10	17	24	31	
4	11	18	25	26	
5	12	19	20	27	
6	13	21	28	29	
7	14	22	29	30	
<p><b>A</b> Total tax liability for first month of quarter ▶ <b>A</b> <b>20782 : 02</b></p>					
<b>B. Daily Tax Liability—Second Month of Quarter</b>					
1	8	15	22	29	
2	9	16	23	30	
3	10	17	24	31	
4	11	18	25	26	
5	12	19	20	27	
6	13	21	28	29	
7	14	22	29	30	
<p><b>B</b> Total tax liability for second month of quarter ▶ <b>B</b> <b>9423 : 74</b></p>					
<b>C. Daily Tax Liability—Third Month of Quarter</b>					
1	8	15	22	29	
2	9	16	23	30	
3	10	17	24	31	
4	11	18	25	26	
5	12	19	20	27	
6	13	21	28	29	
7	14	22	29	30	
<p><b>C</b> Total tax liability for third month of quarter ▶ <b>C</b> <b>11292 : 82</b></p>					
<p><b>D</b> Total for quarter (add lines <b>A</b>, <b>B</b>, and <b>C</b>). This should equal line 13 of Form 941 (or line 10 of Form 941-SS) ▶ <b>D</b> <b>71517 : 18</b></p>					
<p>For Paperwork Reduction Act Notice, see page 2.</p>			<p>Cat. No. 11967Q</p>	<p>Schedule B (Form 941) (Rev. 1-2002)</p>	

# Answers

## Lesson 3, Part 2

### Exercise 1

- (A) \$30,600
- (B) \$244.80
- (C) 5/1/02
- (D) \$11,200
- (E) \$89.60

Mr. Wilson's Business		
Employee	Wages subject to FUTA tax	
	1st qtr.	2nd qtr.
R. Riding	\$4,500	\$2,500
M. Lamb	7,000	—
J. Nimble	3,400	3,400
C. Moon	5,600	1,400
C. Fiddle	4,900	2,100
P. Son	5,200	1,800
Total Wages	\$30,600	\$11,200 (x.008)

- (F) No deposit required for under \$100.
- (G) 90%

### Exercise 2

- (A) 7/31/02
- (B) \$101.60
- (C) \$44.00

See filled-in Exhibit 3.14 page A-7.

**ANSWER TO EXERCISE 2 – EXHIBIT 3.14**

Form <b>940-EZ</b> Department of the Treasury Internal Revenue Service (99)	<b>Employer's Annual Federal                  Unemployment (FUTA) Tax Return</b>	OMB No. 1545-1110 <div style="font-size: 2em; font-weight: bold; text-align: center;">2002</div>
▶ See separate Instructions for Form 940-EZ for information on completing this form.		
You must complete this section. ▶	Name (as distinguished from trade name) <b>ACME, INC.</b> Trade name, if any	Calendar year <b>2002</b>
	Address and ZIP code <b>123 FIRST ST., CEDAR, MI 49621</b>	Employer identification number <b>10:7654321</b>

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Answer the questions under **Who May Use Form 940-EZ** on page 2. If you cannot use Form 940-EZ, you must use Form 940.

**A** Enter the amount of contributions paid to your state unemployment fund. (see separate instructions) . . . ▶ \$ **401 | 40**

**B** (1) Enter the name of the state where you have to pay contributions . . . ▶ **MICHIGAN**  
 (2) Enter your state reporting number as shown on your state unemployment tax return ▶ **12345**

If you will not have to file returns in the future, check here (see **Who Must File** in separate instructions) and complete and sign the return. ▶

If this is an Amended Return, check here (see **Amended Returns** on page 2 of the separate instructions) . . . ▶

**Part I Taxable Wages and FUTA Tax**

1 Total payments (including payments shown on lines 2 and 3) during the calendar year for services of employees	1	26000	00
2 Exempt payments. (Explain all exempt payments, attaching additional sheets if necessary.) ▶	2		
3 Payments of more than \$7,000 for services. Enter only amounts over the first \$7,000 paid to each employee. (see separate instructions) . . . . .	3	7800	00
4 Add lines 2 and 3 . . . . .	4	7800	00
5 Total taxable wages (subtract line 4 from line 1) . . . . .	5	19200	00
6 FUTA tax. Multiply the wages on line 5 by .008 and enter here. (If the result is over \$100, also complete Part II.)	6	145	60
7 Total FUTA tax deposited for the year, including any overpayment applied from a prior year . . . . .	7	101	60
8 Balance due (subtract line 7 from line 6). Pay to the "United States Treasury." . . . . .	8	44	00
9 Overpayment (subtract line 6 from line 7). Check if it is to be: <input type="checkbox"/> Applied to next return or <input type="checkbox"/> Refunded ▶	9		

**Part II Record of Quarterly Federal Unemployment Tax Liability** (Do not include state liability.) Complete only if line 6 is over \$100.

Quarter	First (Jan. 1 – Mar. 31)	Second (Apr. 1 – June 30)	Third (July 1 – Sept. 30)	Fourth (Oct. 1 – Dec. 31)	Total for year
Liability for quarter	52.00	49.60	27.60	16.40	145.60

**Third Party Designee** Do you want to allow another person to discuss this return with the IRS (see instructions page 5)?  Yes. Complete the following.  No

Designee's name ▶ \_\_\_\_\_ Phone no. ▶ ( ) \_\_\_\_\_ Personal identification number (PIN) ▶ \_\_\_\_\_

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and, to the best of my knowledge and belief, it is true, correct, and complete, and that no part of any payment made to a state unemployment fund claimed as a credit was, or is to be, deducted from the payments to employees.

Signature ▶ \_\_\_\_\_ Title (Owner, etc.) ▶ \_\_\_\_\_ Date ▶ \_\_\_\_\_

For Privacy Act and Paperwork Reduction Act Notice, see separate instructions. ▼ DETACH HERE ▼ Cat. No. 10983G Form 940-EZ (2002)

Form <b>940-EZ(V)</b> Department of the Treasury Internal Revenue Service	<b>Form 940-EZ Payment Voucher</b>	OMB No. 1545-1110 <div style="font-size: 2em; font-weight: bold; text-align: center;">2002</div>
Use this voucher only when making a payment with your return.		
Complete boxes 1, 2, and 3. Do not send cash, and do not staple your payment to this voucher. Make your check or money order payable to the "United States Treasury." Be sure to enter your employer identification number, "Form 940-EZ," and "2002" on your payment.		
1 Enter your employer identification number.  <b>10:7654321</b>	2 Enter the amount of your payment. ▶  <div style="text-align: right;">Dollars      Cents</div> <div style="text-align: right; font-size: 1.2em;"><b>44      00</b></div>	3 Enter your business name (individual name for sole proprietors). <b>ACME, INC.</b> Enter your address. <b>123 FIRST ST.</b> Enter your city, state, and ZIP code. <b>CEDAR, MI 49621</b>

# Answers

## Lesson 4

### ANSWER TO EXERCISE – EXHIBIT 4.4

Form <b>8829</b> <small>Department of the Treasury Internal Revenue Service (99)</small>	<b>Expenses for Business Use of Your Home</b> ▶ File only with Schedule C (Form 1040). Use a separate Form 8829 for each home you used for business during the year. ▶ See separate instructions.	OMB No. 1545-1266 <div style="font-size: 2em; font-weight: bold; text-align: center;">2002</div> Attachment Sequence No. 66 Your social security number <b>131 00 0001</b>
Name(s) of proprietor(s) <b>FRANK</b>		
<b>Part I Part of Your Home Used for Business</b>		
1	Area used regularly and exclusively for business, regularly for day care, or for storage of inventory or product samples (see instructions)	280
2	Total area of home	2800
3	Divide line 1 by line 2. Enter the result as a percentage	10 %
• For day-care facilities not used exclusively for business, also complete lines 4-6. • All others, skip lines 4-6 and enter the amount from line 3 on line 7.		
4	Multiply days used for day care during year by hours used per day	hr.
5	Total hours available for use during the year (365 days × 24 hours) (see instructions)	8,760 hr.
6	Divide line 4 by line 5. Enter the result as a decimal amount	6
7	Business percentage. For day-care facilities not used exclusively for business, multiply line 6 by line 3 (enter the result as a percentage). All others, enter the amount from line 3	10 %
<b>Part II Figure Your Allowable Deduction</b>		
8	Enter the amount from Schedule C, line 29, plus any net gain or (loss) derived from the business use of your home and shown on Schedule D or Form 4797. If more than one place of business, see instructions. See instructions for columns (a) and (b) before completing lines 9-20.	30,000 00
	(a) Direct expenses      (b) Indirect expenses	
9	Casualty losses (see instructions)	
10	Deductible mortgage interest (see instructions)	10,000 00
11	Real estate taxes (see instructions)	2,500 00
12	Add lines 9, 10, and 11	12,500 00
13	Multiply line 12, column (b) by line 7	13
14	Add line 12, column (a) and line 13	1,250 00
15	Subtract line 14 from line 8. If zero or less, enter -0-	28,750 00
16	Excess mortgage interest (see instructions)	
17	Insurance	500 00
18	Repairs and maintenance	200 00
19	Utilities	2,200 00
20	Other expenses (see instructions)	
21	Add lines 16 through 20	4,700 00
22	Multiply line 21, column (b) by line 7	470 00
23	Carryover of operating expenses from 2001 Form 8829, line 41	
24	Add line 21 in column (a), line 22, and line 23	670 00
25	Allowable operating expenses. Enter the smaller of line 15 or line 24	670 00
26	Limit on excess casualty losses and depreciation. Subtract line 25 from line 15	28,080 00
27	Excess casualty losses (see instructions)	
28	Depreciation of your home from Part III below	517 00
29	Carryover of excess casualty losses and depreciation from 2001 Form 8829, line 42	
30	Add lines 27 through 29	517 00
31	Allowable excess casualty losses and depreciation. Enter the smaller of line 26 or line 30	517 00
32	Add lines 14, 25, and 31	2,437 00
33	Casualty loss portion, if any, from lines 14 and 31. Carry amount to Form 4684, Section B	
34	Allowable expenses for business use of your home. Subtract line 33 from line 32. Enter here and on Schedule C, line 30. If your home was used for more than one business, see instructions	2,437 00
<b>Part III Depreciation of Your Home</b>		
35	Enter the smaller of your home's adjusted basis or its fair market value (see instructions)	250,000 00
36	Value of land included on line 35	40,000 00
37	Basis of building. Subtract line 36 from line 35	210,000 00
38	Business basis of building. Multiply line 37 by line 7	21,000 00
39	Depreciation percentage (see instructions)	2.461 %
40	Depreciation allowable (see instructions). Multiply line 38 by line 39. Enter here and on line 28 above	517 00
<b>Part IV Carryover of Unallowed Expenses to 2003</b>		
41	Operating expenses. Subtract line 25 from line 24. If less than zero, enter -0-	
42	Excess casualty losses and depreciation. Subtract line 31 from line 30. If less than zero, enter -0-	

For Paperwork Reduction Act Notice, see page 4 of separate instructions.

Cat. No. 13232M

Form 8829 (2002)

