

Individual Federal Income Tax

GROSS Income --	\$100,000	[tax ≈ \$20,000]
minus personal EXEMPTIONS @ \$3500 [family of Mom and 2 kids]	≈ \$10,000	
minus standard or itemized DEDUCTIONS [state/local tax, mortgage %, charity, etc.]	≈ \$20,000	
equals TAXABLE income --	\$70,000	tax = \$13,000

Adding “Schedule C” Business-Related Deductions from Biz Income

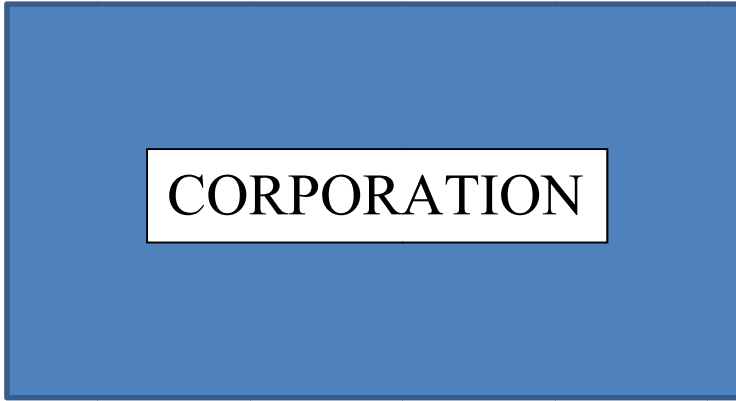
GROSS Income --	\$100,000	[tax ≈ \$20,000]
<i>BUSINESS-ONLY deductions:</i>		
\$20,000 wages to an employee		
\$10,000 rent for her storefront		
\$2000 office supplies		
\$1500 business insurance		
\$1000 electricity, water and other utilities		
\$500 advertising and business travel		
\$3000 interest on business loan of any kind		
\$2000 “depreciation” on truck used in biz		
	TOTAL = \$40,000	
NET business income =	\$60,000	
minus personal EXEMPTIONS @ \$3500 [family of Mom and 2 kids]	≈ \$10,000	
minus standard or itemized DEDUCTIONS [state/local tax, mortgage %, charity, etc.]	≈ \$20,000	
equals TAXABLE income --	\$30,000	tax = \$4000

SOLE PROPRIETORSHIP = sole proprietor/business person

business tax = personal tax

Corporate Double-Taxation and “Sub-chapter C”

GROSS Income -- \$100,000



Biz DEDUCTIONS

\$20,000 wages to an employee
 \$10,000 rent
 \$2000 office supplies
 \$1500 business insurance
 \$1000 utilities
 \$500 advertising, business travel
 \$3000 interest on business loan
 \$2000 “depreciation” on truck
 TOTAL = \$40,000

NET business income = \$60,000 → corporate tax = **\$9000**

IF THE CORP PAYS A DIVIDEND



SHAREHOLDER(S)

net dividend to shareholder(s) -- \$51,000 ←

minus personal EXEMPTIONS ≈ \$10,000

minus personal itemized DEDUCTIONS ≈ \$20,000

equals personal TAXABLE income -- \$21,000 15% “**capital gains**” inc. tax = **\$3150**

Total “double tax” = \$9000 corp tax + \$3150 capital gains tax = \$12,150

TRIPLE the tax of the individual sole proprietor!

Partnership Pass-Through Taxation and “Sub-chapter K”

GROSS Income -- \$100,000

Business DEDUCTIONS

\$20,000 wages to an employee
 \$10,000 rent
 \$2000 office supplies
 \$1500 business insurance
 \$1000 utilities
 \$500 advertising, business travel
 \$3000 interest on business loan
 \$2000 “depreciation” on truck
TOTAL = \$40,000



PARTNERSHIP

ALL income and deductions (profits/losses)
pass through partnership
 and **allocated** to partners
 ... whether or not cash is actually **distributed** ...



PARTNERS

NET TAXABLE business income =	\$60,000	
minus personal EXEMPTIONS	≈ \$10,000	
minus personal itemized DEDUCTIONS	≈ \$20,000	
equals personal TAXABLE income --	\$30,000	personal income tax = \$4000

Almost \$10,000 less (1/3) same scenario with C-corp double tax . . .

Corporation Pass-Through Taxation and “Sub-chapter S”

S-Corporation taxed largely as a partnership (some differences), but . . .

- unanimous shareholder election of S-Corporation status within 2 months of formation
- no more than 100 shareholders
- shareholders = no nonresident aliens, no non-natural (juridical) entities other than trusts
- classes of stock only for voting differences (no financial, management differentiation)

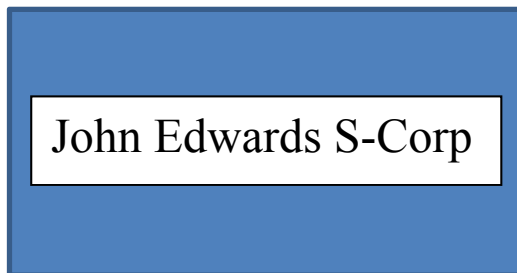
Limited Liability Companies *Choose* **Pass-Through Taxation (or not): “Check the Box”**

Self-Employment Tax

GROSS Income --	\$100,000	
minus business DEDUCTIONS	= \$40,000	
minus personal EXEMPTIONS	≈ \$10,000	
minus personal itemized DEDUCTIONS	≈ \$20,000	
equals TAXABLE income --	\$30,000	INCOME tax = \$4000
+ SE tax = 15.3% of \$60,000 net biz income = \$9180		TOTAL TAX = \$13,180
<i>12.4% Social Security up to \$110,000 + 2.9% Medicare unlimited</i>		

MORE THAN DOUBLE THE “INCOME” TAX!

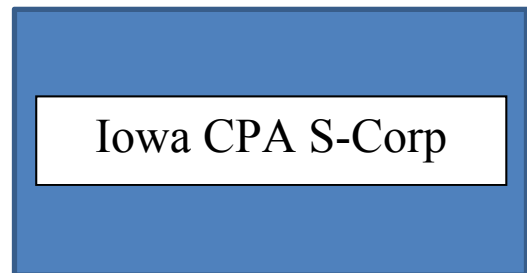
- Tax assessed on “*active*” self-employment “compensation,” but NOT “dividends” . . .
- \$ to LLC members with management authority or 500 hrs service = active = “*compensation*”
- ** \$ to S-corporation shareholders = compensation *only if so designated* “reasonably”



\$7 million annual income pass-through . . .

- \$360,000 called “salary” [avg. NC injury lawyer]
- \$6.64 million “dividend”, *no SE tax!*

[\$6.64 million X 2.9% Medicare = \$192,560/year]



\$200,000 annual income pass-thru

- \$24,000 called “salary”
- \$176,000 “dividend”, no SE tax

\$86,000 X 12.4% Social Security
+ \$176,000 X 2.9% Medicare
= \$10,664 + \$5104 = \$15,768/year

** salary IRS-reset at \$94,000 ...
\$106,000 still sheltered from SE tax
[\$16,000 X 12.4% Social Security +
\$106,000 X 2.9% Medicare =
\$5058/year]