



Biz Hippo

Tax Planning for Real Estate Agents

Takeaways for today

- Understand what deductions you can take in your business
- Understand Self-Employment Tax
- Understand Estimated Taxes
- Sole Proprietorship v. LLC v. S-Corp

Handouts and List of Resources available at bizhippo.com/realestate

**You are not an
employee, you are a
business**

Business Income

So any money you receive from running this business is **income** to you.

- Commissions
- Referral fees from realtors or other service providers
- Any money you receive from almost anyone

Business Deductions

Business Deductions

But, you get to offset that income with your business deductions.

The IRS says an expense must be **“Ordinary and Necessary”** to be deductible.

Ordinary - one that is common and accepted in your industry.

Necessary- helpful and appropriate for your trade or business. Does not have to be indispensable.

Business Deduction Examples

Deductible

- Cell phone
- Business cards
- Advertising
- Realtor License Fees
- Mileage OR Car Expenses *
- Car Wifi or Mobile Hotspot
- Client gifts
- Home office expenses *
- Logo'ed apparel
- Meals with clients or referrers
- Sponsorships

*More information later

Not Deductible

- Clothing
- Down payment on your car
- Meals for just you
- Personal expenses

Documentation Requirements

- When you claim a deduction on your tax return, you are saying to the IRS “I can substantiate this claim with documentation.”
- That documentation needs to be a **invoice or receipt** and some **proof that it was paid** (bank statement, credit card statement).
- Keep documentation for 5 years in case of an audit.
- Digital records are fine.

Recording keeping software:

Quickbooks Freelancer (Self-Employed) - \$12 / month

Freshbooks Lite- \$12 / month

Deductions with Special Rules

Auto Expenses

1. Must keep “contemporaneous records” of business use (use a mileage app on your phone)
2. Can deduct \$0.585 per business mile (2022) OR
3. Business-use percentage of actual expenses (insurance, licenses, gas, lease, payments, repairs, depreciation)- usually results in bigger deduction. See keep track of all auto expenses!
4. Depreciation is complicated- depends on weight of vehicle (< 6000 lbs is a car, > 6000 lbs is a truck), > \$19,000 auto is considered “luxury”. To use accelerated or bonus depreciation, usually must use the car for 50% or more for business. And depreciation lowers the “basis” of your car, which could result in a gain when you trade-in or sell.

See IRS Publication 463 Travel, Gift, and Car Expenses for more information. (irs.gov)

Deductions with Special Rules

Home Office Expenses

1. Home office must be your primary place of business (can't have another office)
2. Must be used exclusively and regularly for business (segregate off a portion of a room)
3. Can deduct a percentage of expenses based on square footage used for office / total square footage of home
4. Expenses include: mortgage interest, rent, insurance, utilities, repairs, maintenance, depreciation.
5. Simplified method is \$5 / sq ft up to a maximum of \$1,500.

See IRS Form 8829 Expenses for Business Use of Your Home for more information. ([irs.gov](https://www.irs.gov))

Self-Employment Tax

16	Tax (see Instructions). Check if any from Form(s): 1 <input type="checkbox"/> 9914 2 <input type="checkbox"/> 4972 3 <input type="checkbox"/>	16	
17	Amount from Schedule 2, line 3	17	
18	Add lines 16 and 17	18	
19	Nonrefundable child tax credit or credit for other dependents from Schedule 8812	19	
20	Amount from Schedule 3, line 8	20	
21	Add lines 19 and 20	21	
22	Subtract line 21 from line 18. If zero or less, enter -0-	22	
23	Other taxes, including self-employment tax, from Schedule 2, line 21	23	
24	Add lines 22 and 23. This is your total tax	24	
25	Federal income tax withheld from:		
a	Form(s) W-2	25a	
b	Form(s) 1099	25b	
c	Other forms (see Instructions)	25c	
d	Add lines 25a through 25c	25d	
26	2021 estimated tax payments and amount applied from 2020 return	26	
27a	Earned Income credit (EIC)	27a	
	Check here if you were born after January 1, 1998, and before January 2, 2004, and you satisfy all the other requirements for taxpayers who are at least age 18, to claim the EIC. See Instructions <input type="checkbox"/>		
b	Nontaxable combat pay election	27b	
c	Prior year (2019) earned income	27c	
28	Refundable child tax credit or additional child tax credit from Schedule 8812	28	
29	American opportunity credit from Form 8863, line 8	29	
30	Recovery rebate credit. See Instructions	30	
31	Amount from Schedule 3, line 15	31	
32	Add lines 27a and 28 through 31. These are your total other payments and refundable credits	32	
33	Add lines 25d, 26, and 32. These are your total payments	33	
Refund	34 If line 33 is more than line 24, subtract line 24 from line 33. This is the amount you overpaid	34	
35a	Amount of line 34 you want refunded to you. If Form 8888 is attached, check here <input type="checkbox"/>	35a	
Direct deposit?	See Instructions.		
b	Routing number	c	Type: <input type="checkbox"/> Checking <input type="checkbox"/> Savings
d	Account number		
36	Amount of line 34 you want applied to your 2022 estimated tax	36	
Amount You Owe	37 Amount you owe. Subtract line 36 from line 24. For details on how to pay, see Instructions	37	
38	Estimated tax penalty (see Instructions)	38	
Third Party Designee	Do you want to allow another person to discuss this return with the IRS? See Instructions <input type="checkbox"/> Yes. Complete below. <input type="checkbox"/> No		
	Designee's name	Phone no.	Personal identification number (PIN)
Sign Here	Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, they are true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.		
	Your signature	Date	Your occupation
			If the IRS sent you an Identity Protection PIN, enter it here (see Inst.)
Joint return? See Instructions. Keep a copy for your records.	Spouse's signature. If a joint return, both must sign.	Date	Spouse's occupation
			If the IRS sent your spouse an Identity Protection PIN, enter it here (see Inst.)

Line 23.
Other taxes:
15.3% of your
profit in
addition to
your income
tax (22-24%)

What are Self-Employment (SE) Taxes?

Federal Insurance Contributions Act (FICA) of 1935 funds Social Security and Medicare	
Social Security Tax aka OASDI Old Age, Survivors, and Disability Insurance	Medicare tax aka hospital insurance
Employees pay 6.2%	Employees pay 1.45%
Employers pay 6.2%	Employers pay 1.45%
Self-employed pay 12.4%	Self-employed pay 2.9%

Social Security tax paid on first \$147,000 of wages or income; Medicare tax has no cap

What are Self-Employment (SE) Taxes?

You've seen them on a paycheck, but you never had to report them on your tax return before. And your employer paid half.

½ of SE Tax does reduce your taxable income to help compensate.

Employee Info		SSN	Pay Schedule	Pay Period	Pay Date		
John Smith (Emp.ID: STS001) 102 Main Street, Anytown, NY 10000.		XXX-XX-7889	Weekly	Feb 19, 2020 to Feb 25, 2020	Feb 26, 2020		
Earnings	Rate	Hours	Total	YTD	Taxes / Deductions	Current	YTD
Regular Earnings	\$10.00	40 hrs	\$400.00	\$400.00	Federal Withholding	\$44.50	\$400.50
					FICA - Social Security	\$24.80	\$223.20
					FICA - Medicare	\$5.80	\$52.20
					State Withholding	\$20.00	\$180.00
					Employer Taxes		
					FUTA	\$24.80	\$223.20
					SUTA	\$44.50	\$400.50
YTD Gross	YTD Taxes / Deductions	YTD Net Pay	Gross	Taxes / Deductions	Net Pay		
\$3,600.00	\$855.90	\$2,744.10	\$495.00	\$410.00	\$744.10		

When Estimating Taxes, Don't Overlook SE Taxes

In addition to income tax, add 15.3% of income for SE Taxes to your estimates.

If you anticipate making more than \$147,000 (the social security wage limit), add \$18,228 + 2.9% of income to your estimates.

See IRS Form SE (Form 1040) Self-Employment Tax ([irs.gov](https://www.irs.gov))

Estimated Taxes

These are **ESTIMATES**

Tax Estimates are due on **April 15, July 15, September 15 and January 15**. The IRS wants / requires / requests you to pay your taxes throughout the year.

To avoid any underpayment penalty, you need to pay in **100% of last year's tax or 90% of your current year tax**. Referred to as the “safe harbor”

Easiest way to make payments is through **EFTPS.gov**. You will be mailed a PIN number, so set up a few weeks before you want to use it. Arkansas uses [https://atap.arkansas.gov/ /](https://atap.arkansas.gov/)

BUT... you don't know how much tax you will owe in the current year.

AND... the IRS doesn't either- until you file your tax return.

AND... is the underpayment penalty that horrible?

Underpayment Penalty

Roughly, the IRS takes the amount you owe, divides by 4, and computes interest on any underpayment for that quarter.

If your income is not earned consistently throughout the year, particularly if most of your income is later in the year, you may benefit by using the **Annual Income Installment Method**. You just need to know what you earned each quarter.

What's the interest rate they charge?

See IRS Publication 505, Tax Withholding and Estimated Tax and Form 2210 Underpayment of Estimated Tax by Individuals, Estates, and Trusts (irs.gov)

Underpayment Penalty Rates

Year	Q1	Q2	Q3	Q4
2022	3%			
2021	3%	3%	3%	3%
2020	5%	5%	3%	3%
2019	6%	6%	5%	5%

Estimated Taxes Summary

I would pay **estimated taxes each quarter based on your earnings for that quarter at 37%**. (22% income tax + 15.3% SE tax). In the 4th quarter, you can look at what you have paid in and adjust accordingly.

If you have the money, pay it in. You don't want to scramble to find money in April.

However, I would **err on the side of underpaying**. You can't get any overpayment back until you file your tax return.

DON'T PANIC about estimated taxes. They are ESTIMATES and if you miscalculate, you will only be charged 3% at the current rates- not life-changing.

LLC? S-Corp?

What's this LLC / S-Corp Nonsense?

Without forming a separate entity, you are considered a **sole proprietor**. You and your business are the same person.

If you file with the state to **create an entity (Limited Liability Company, Corporation, Partnership)** you have created a separate entity. Now there is a business entity and you, a person.

Why would you do that?

See www.sos.arkansas.gov/ Arkansas Secretary of State Website for creating business entities

Sole Proprietor-
you and
business are
one

The diagram consists of three overlapping circles. A large light green circle at the top contains the text 'Sole Proprietor- you and business are one'. Below it, two smaller circles overlap: a light green circle on the left containing 'Business Entity (LLC, Corp, Partnership)' and a dark grey circle on the right containing 'You, the person'.

Business Entity
(LLC, Corp,
Partnership)

You, the
person

It CAN limit your personal liability

LLC's and Corporations can limit your personal liability (protect your personal assets) from:

- car accidents
- acts of employee or contractors
- General liability claims

LLC's and Corporations MAY NOT limit your personal liability related to your professional license

- breach of contract
- unethical, fraudulent acts



Note: Partnerships do not limit your liability unless you are a limited partner

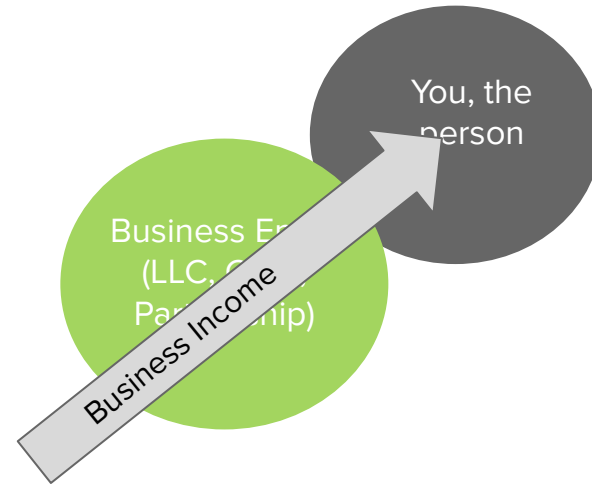
What does an Entity mean to the IRS?

In many cases, the IRS barely acknowledges the separate entity. These entities are called **Pass-Through Entities** and it means the income flows through to the owner, where it is taxed at the individual level.

Pass-through entities include LLC's, Partnerships and S-Corporations.

Single-member LLC's don't even have to file their own tax return. It is reported on the Schedule C on your personal return- just like a sole proprietorship.

The LLC has no tax advantage over a sole proprietorship.



Required Tax Filings by Entity

Entity Type	Business Tax Return	Reported on Form 1040
Sole Proprietorship	None	Schedule C
Limited Liability Company- single member	None	Schedule C
Limited Liability Company- > 1 member	Form 1065 Partnership Tax Return	Schedule E
Partnership	Form 1065 Partnership Tax Return	Schedule E
S-Corporation	Form 1120S S-Corporation Tax Return	Schedule E

LLC v. S-Corporation

The Secretary of State of your state and the IRS can see your entity differently.

Therefore, you can elect with the IRS to have your entity taxed in different ways.

Thus, the S-Corporation Election.

Arkansas Secretary
of State sees



IRS sees



Difference between an LLC & S-Corp

LLC	S-Corp
Business Income subject to Self-Employment Tax	Business Income NOT subject to Self-Employment Tax
If single member, entity does not file a separate tax return	Entity always files Form 1120S regardless of number of members
Cash taken out of company usually as distributions only- no salary requirements	Owner must be paid "reasonable compensation" for services provided to the company

Electing to be taxed as an S-Corp

- Probably not worth it if your business income is less than \$90,000
- File the election when you create the entity OR during the first 75 days of the year (March 15) to avoid having two filings for the year.
- You can only change your status with the IRS every 5 years.
- You will have to start paying yourself through payroll. (I recommend Gusto payroll platform)
- No requirement to pay salary evenly throughout the year.
- Reasonable compensation is not well-defined. It will depend on how much your business makes and comparable salaries at other businesses.
- Form 8832 Entity Classification Election and Form 2553 Election by a Small Business Corporation are how you elect to be taxed as an S-Corporation. Send them together to the IRS.

Forming an Entity

- Must have an **Operating Agreement & Articles of Organization** for your Entity (If more than one member, consult an attorney. Otherwise, you can use a template for both.)
- **File the “Certificate of Organization of Domestic LLC”** at <https://www.ark.org/sos/corpfilings/index.php> Arkansas Secretary of State. Filing fee \$50. (Registered Agent? It can be you as an individual. Must have a real street address- no PO box.)
- **Get an Employer Identification Number at www.irs.gov.** (You will need to provide your Social Security number as the responsible party. When asked about wages, enter that you do not plan to pay any. Otherwise, the IRS will expect a quarterly payroll tax return.)
- If **electing S-Corp status**, file Form 8832 Entity Classification Election and 2553 Election by a Small Business Corporation. Send them together to the IRS.

Getting Ready for Payroll

- **Must have an EIN** (Employer Identification Number) for your entity.
- Get an **Arkansas Employer withholding number** at <https://ATAP.arkansas.gov> under “Register New Business”
- Get an **ADWS Employer Account Number** for Arkansas Unemployment. <https://www.dws.arkansas.gov/employers/ui-employer-services/>
- Set up your payroll with a **payroll service provider** (I recommend Gusto.com)

Summary

- Take all deductions available to you- keep records
- Don't forget to include Self-Employment tax in your estimates
- Understand Estimated Taxes and don't panic about them
- Sole Proprietorship v. LLC v. S-Corp

Handouts and List of Resources available at bizhippo.com/realestate