

WELCOME TO  
Bradford and Company Inc.'s

**TAX**  
**STRATEGIES**  
for the  
**Self-Employed**

Presented by  
Ron Reed, CPA



## **Your Speaker: Ron Reed, CPA**

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Ron is regarded as one of America's foremost experts on tax-saving strategies for self-employed business owners. Since 1980, Ron has presented more than 2,000 seminars on tax strategies to over 300,000 real estate agents, insurance agents, financial planners, attorneys, CPAs, and doctors.

Ron is a former Green Beret who spent five years as a tax specialist with the international accounting firm of Price Waterhouse in its Phoenix office; six years as the vice president and director of taxes for Combined Communications Corp., a Fortune 500 company; and six years as the vice president of the Tax Reduction Institute.

Currently Ron is on the senior faculty of the Becker Professional Review, an international educational company that prepares college graduates to pass the CPA examination, and is an instructor for Bradford and Company, Inc.'s tax strategy courses.

Student evaluations from over 4,500 presentations to accounting graduates preparing for the CPA exam rank Ron in the top 5% of over 500 instructors, and often in the top 1%.

Born in Crete, Nebraska in 1945, Ron and his family moved to Scottsdale, Arizona from Lincoln, Nebraska in 1960. Ron, his wife Charlet, and their children and grandchildren all live in the Phoenix Metropolitan Area.

Ron and Murray Bradford co-authored the national best-selling *Business Tax Deduction Master Guide* published by Prentice-Hall in 1980. Ron is a contributing editor to the Tax Reduction Letter, a monthly tax and financial newsletter.

Ron was selected as the national media representative for the J.K. Lasser Institute, publisher of *J.K. Lasser's Your Federal Income Tax*. He completed a 13-city book promotion tour; including appearances on 13 television stations and 21 radio stations, and articles published in 9 newspapers. Also appeared on Good Morning America, CNN, and Financial News Network.

He is a past president of the Central Arizona Chapter of CPAs and Vice President of the Arizona Society of CPAs.



## **W. Murray Bradford, CPA, Founder & President of Bradford and Company, Inc.**

With more than 35 years of experience as a CPA, and more than 25 years helping the self employed optimize their income taxes, W. Murray Bradford is the nation's pre-eminent tax reduction expert. Since he began aiding the self employed, Murray's tax strategies have helped more than 500,000 people find an average of \$17,700 in new tax deductions.

### **The Tax Reduction Expert**

Mr. Bradford's CPA experience is anchored by nine years with the international accounting firm Price Waterhouse. At Price Waterhouse, Mr. Bradford enjoyed the elite distinction of being selected from thousands for two tours of duty in the firm's

Washington, D.C. national office.

Mr. Bradford was also named a Top Instructor at the Becker CPA Review Course for 15 years.

Mr. Bradford's tax expertise has helped him author many publications, including:

- *Tax Strategies for the Self-Employed*
- *The Prentice Hall Business Tax Deduction Master Guide*
- *Business Tax Deduction Master Guide*
- *Income Tax Reduction Strategies for Property Owners*
- *Tax Aspects of Financial Planning*

Mr. Bradford is an active member of the American Institute of Certified Public Accountants, the California Society of CPAs, the Minnesota Society of CPAs, and the Greater Washington, D.C. Society of CPAs.

Mr. Bradford helps keep the self employed community informed with appearances on many different media outlets: CBS News Nightwatch, Financial News Network, KCBS, KGO-TV, Fox, and NPR.

Mr. Bradford is quoted in many financial publications, including: *The Wall Street Journal*, *The New York Times*, *Changing Times*, *Money*, *Fortune*, and *USA Today*

A former Marine, Mr. Bradford received his accounting degree from the University of Wisconsin, Superior. Bradford and Company, Inc. was founded in Washington, D.C. In 1995, Mr. Bradford moved the firm to Northern California's Bay Area, where the corporate headquarters remain today, albeit the firm retains research abilities in the Washington D.C. area.

# Suggestion

## Use a CPA or EA to Prepare Your Tax Returns and File an Extension

1. Having a CPA or EA prepare and sign your return will reduce your audit risk and assist you in implementing tax strategies
2. If they are an Enrolled Agent (“EA”), did they pass the Special Enrollment Examination administered by the U.S. Department of the Treasury or did they qualify by working for the IRS
3. **Select a CPA or EA just like you:** do they operate as a sole proprietor, limited liability company, or corporation (S or C); are they married or single; are they about your age; have they been in business about the same time as you; do they work out of their home or an outside office; do they have employees
4. **Other factors to consider:** do they have other self-employed clients; do they have other clients in your profession or business; do they attend continuing education courses about tax strategies for the self-employed; are they licensed to sell insurance, mutual funds, or stocks
5. Make certain they subscribe to a Web-based tax research service
6. Extending your return will allow you to meet with them after their busy season when they will be rested and working regular hours; the IRS selects a higher percentage of returns to audit that are filed on or before the original due date
7. To avoid penalties and interest, make the required quarterly estimated payments and any additional tax that may be required on or before the original due date of your return

*Notes and Questions:*

# Suggestion

## Know Your Tax Bracket – Federal, State and Self-Employment

1. Federal tax brackets:

### 2011 Tax Brackets

Tax Rate	Single	Married Filing Jointly
10%	Not over \$8,500	Not over \$17,000
15%	\$8,500 - \$34,500	\$17,000 - \$69,000
25%	\$34,500 - \$83,600	\$69,000 - \$139,350
28%	\$83,600 - \$174,400	\$139,350 - \$212,300
33%	\$174,400 - \$379,150	\$212,300 - \$379,150
35%	Over \$379,150	Over \$379,150

2. Self-Employment tax is 13.3% (10.4% Social Security and 2.9% Medicare)
3. Social Security tax on wages or net earnings to a maximum of \$106,800 in 2011
4. Medicare tax on wages or net earnings without limitation
5. **Your tax bracket is the percent of tax paid on the last “business dollar earned”**

*Notes and Questions:*

# Suggestion

## Use Your Appointment Book as a Diary of Your Business Activities and a Record of Your Expenses

1. Use your appointment system to keep a detailed record of your business activities – **Business activities generate business deductions**
2. Make a copy of your appointments and business activities each month for your tax records
3. Generally, all business deductions must be supported by both a receipt and proof of payment (check or credit card)
4. Generally, you do not need a receipt for vehicle, entertainment, and travel (other than lodging) expenses under \$75; **however, travel, vehicle, home office and entertainment expenses have specific documentation requirements for deduction (use a hand written diary to record these types of expenses)**
5. **Owner/shareholders of corporations are employees and should submit an Employee Reimbursement Form for business expenses paid by cash, personal checks and personal credit cards**
6. You only need to keep track of your business deductions; put them in a “category” (entertainment, office rent, supplies, etc.) and accumulated the totals for the year
7. Four easy ways to accumulate your deductions:
  - a. Paper and pencil
  - b. Excel spreadsheet
  - c. Quicken software
  - d. Quick Books (Generates a Balance Sheet)

*Notes and Questions:*

# Tax Strategy

## Deduct Dutch-Treat Entertainment

1. **Entertainment** = FUN (IRS definition)
2. Entertainment includes: meals at restaurants and home, drinks, golf, tennis, sporting events, movies, and theatre
3. Under \$75 no receipt required (record in your diary)
4. Only 50% ends as a deduction (your tax return eats the other part)
5. **Directly Related Entertainment** requires a business setting (tables and chairs)
6. **Associated Entertainment** (non-business setting) must be associated with Directly Related Entertainment (before or after)
7. Who, What, When, Where, Why and How Much (Using a credit card documents When, Where and How Much)
8. Prospects, Referrals, and Colleagues

Dutch-Treat: Reg. Section 1.274-2(b)(1)(i) & (ii)

\$75 Receipt Rule: Reg. Section 1.274-5T(c)(2)(iii)(B)

Prospects and Referrals: Charles F. Urbauer, T.C. Memo. 1992-170

Colleagues: James M. O'Donoghue (Laurie), 47 T.C.M. 1563 (1984)

*Notes and Questions:*

# Tax Strategy

## Deduct Entertaining at Home

1. Home entertainment is deductible as either directly related or associated entertainment
2. To document the cost, visit the grocery store and buy everything you will need to feed and entertain your business guests
3. If the total purchased is \$75 or more, you will need a receipt
4. Add a “kicker” of 10-15% to cover the cost of food, beverage and other items that you use from your existing supplies

*Notes and Questions:*

# Tax Strategy

## Deduct 100% of Special Sporting Events

1. Golf and tennis tournaments that are organized for the primary purpose of benefiting a charity
2. Gives the entire proceeds to charity
3. Uses volunteers to perform substantially all of the event's work
4. PGA golf tournaments qualify
5. Local charity events qualify
6. Deduction includes the cost of the ticket package, including amounts paid for seating, use of entertainment areas, contestant positions, meals furnished at or as part of the event, and parking

Special "sporting events": IRC Section 274(I)

*Notes and Questions:*

# Tax Strategy

## Claim Your Home Office as Your Principal Place of Business

1. Claiming a Home Office Deduction **does not “trigger”** an audit (use IRS Form 8829)
2. The IRS told Congress that the new rules included in the 1997 Tax Reform Act would allow more than 20 million taxpayers to qualify their home office as their principal place of business; therefore, Congress postponed the effective date until January 1, 1999
3. **Deduct business portion of mortgage interest, property taxes, utilities, homeowner’s insurance, repairs, pest control and depreciation or rent**
4. Depreciate over 39 years using straight-line method
5. Basis of home is the “Lower of Cost or Market” excluding the amount allocated to land
6. Deduct 100% of repairs to office area
7. Eliminates commuting so your business vehicle is more deductible (IRS Publication 17, page 181)
8. **Administrative or management duties = principal office, effective January 1, 1999** (IRS Publication 587, page 3)
9. Exclusive and regular use is required (regular use = 10 hours or more per week)
10. Document regular use 90 days each year
11. Take photographs to prove you have an office in your home
12. **Employee must meet convenience of employer requirement (applies to owner/shareholder of a corporation)**
13. Does not affect tax exempt gain on sale (December 24, 2002)
14. Depreciation after May 6, 1997 is recaptured at capital gains rates
15. Business use is based on the square footage method or any other reasonable method
16. If Schedule C shows a loss before deducting the Home Office, mortgage interest and real estate taxes are still deductible, but operating expenses must be carried forward

Regular Use equals 10 hours or more: Green v. Commr., 78 T.C. 428 (1982)

*Notes and Questions:*

# Administrative Office

There are many activities that are administrative or managerial in nature. The following are a few examples. (IRS Publication 587, pages 3-5)

- Billing customers, clients, or patients
- Keeping books and records
- Ordering supplies
- Setting up appointments
- Forwarding orders or writing reports

Example 1 – John is a self-employed plumber. He has a small office in his home that he uses to phone customers, order supplies, and keep his books.

Example 3 – Paul 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 an office where he could do administrative or management activities.

Paul very rarely uses the office the hospital provides. He uses a room in his home that he has converted to an office. He uses the room to conduct 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
- Reading medical journals and books

## Overview Calculation of Home Office Monetary Benefits

	Gross	% Office	Deduction	Tax Rate	Cash
Mortgage interest	\$15,400	17%	\$2,618	15.3%	\$401
Property taxes	1,500	17%	255	15.3%	39
Utilities	2,105	17%	358	47.8%	171
Homeowner's ins.	317	17%	54	47.8%	26
Repairs, paint, etc.	800	17%	136	47.8%	65
Pest control	480	17%	82	47.8%	39
Repairs to office part	230	100%	230	47.8%	110
Depreciation - equip	1,350	100%	1,350	47.8%	645
Depreciation - home	6,800	17%	1,156	47.8%	553
Cash from the home office deduction					2,049
Eliminate 9-mile commute			3,150	47.8%	1,506
Annual cash from office and vehicle					<u>\$3,555</u>

25% federal taxes, 7.5% state taxes, and 15.3% self-employment taxes make up the 47.8% rate

## Eliminates Commuting and Takes Advantage of Your Living Costs

The administrative home office eliminates commuting. Smith, our example taxpayer, erases 9 miles of commute a day. That's 18 miles round trip, 90 miles a week, 4,500 miles a year converted from ugly personal to beautiful business miles. In Smith's case, the 4,500 miles increased his car deductions by \$3,150 a year.

You need a place to live—why not deduct part of that place? It makes no difference if you own or rent. With the home office deduction, you convert otherwise personal expenses to business deductions.

Most of these expenses are expenses you have no matter what. Mortgage interest, property taxes, utilities, homeowners insurance, pest control, repairs, and paint are all common home expenses.

Extra benefits from mortgage interest: On the mortgage interest you already pay, you convert the home office part (17 percent in this case) to business and deduct it against your self-employment income. If your business income is:

- Under the Social Security maximum, you gain 15.3 percent in extra tax benefits.
- Over the Social Security maximum, you gain 2.9 percent Medicare tax benefit.

More cash from the phaseouts: Then, no matter if you are over or under the Social Security maximum, you gain on those sneaky phaseout taxes that apply to:

- Reducing your itemized deductions
- Reducing your personal exemptions
- Limiting your real estate rental deductions
- Cutting back your child credits

The phaseout tax benefits alone could produce 20 percent or more in benefits depending on your situation. To calculate the true after-tax benefit in your individual case, do your tax return two ways—with and without the home office and vehicle benefits.

Cash benefits from depreciation: Depreciation on this home produces \$553 in annual after-tax cash benefits. When Smith sells, he will pay a recapture tax of \$289 (25 percent x \$1,156), pocketing \$264 on the depreciation deduction.

Claim office until death: When you die, the law forgives the home office and marks up the home to fair market value for estate tax purposes. The markup for estate tax purposes does not trigger any depreciation recapture or capital gains taxes on the death transfer (assuming you die before 2010).

# Tax Strategy

## The Only Legal Way for Your Corporation to Claim a Home Office Deduction

**Step one:** Have your corporation tell you in writing that you need to find an office for the convenience of the corporation.

**Step two:** On or before December 31, complete IRS Form 8829 as if you personally were going to claim a deduction for an office in your home.

**Step three:** On or before December 31, submit your completed Form 8829 to your corporation. Next, have your corporation reimburse the deduction amount shown on IRS Form 8829. The amount reimbursed is a deduction on the corporate books. You receive this reimbursement tax-free (it's a reimbursed employee expense to you).

By doing the home office deduction using the three steps above, you gain the five benefits below:

1. You avoid the miscellaneous deductions category where the total of these miscellaneous deductions get reduced by the 2 percent of adjusted gross income floor.
2. You avoid losing the home office deduction to the alternative minimum tax.
3. You avoid the no-renting-to-your-employer rule.
4. You win by getting the total home-office deduction at the corporate level.
5. You legally hide the home-office deduction from the IRS (it shows as office expenses in the corporate return and does not appear at all on your personal return).

Leslie A. Roy v Commr., T.C. Memo 1998-125

PLR 8819009; CCA 200121070

Bradford Tax Institute Website: November 2008 Tax Reduction Letter

*Notes and Questions:*

# Tax Strategy

## Document Mileage Using the 90-day Test

1. A daily mileage log is required to deduct the business use of a vehicle (IRS or actual method)
2. Commuting to your principal place of business is not deductible
3. **Remember commuting is eliminated if your home office is your principal place of business**
4. Record beginning and ending odometer each year (required by law)
5. **Record beginning odometer mileage every day for 90 days in a row** (Reg. Section 1.274-5T(c)(3)(ii)(c), Example 1)
6. Keep track of business, personal, and commuting mileage for 90 days and then use these results to compute the business percentage to use for entire year

*Notes and Questions:*

# Tax Strategy

## Use IRS Mileage Rates or Actual Expenses Whichever is Greater

1. 51 cents per business mile January 1, 2011 to June 30, 2011 and 55.5 cents July 1, 2011 to December 31, 2011
2. **IRS mileage rates are based on a “composite” automobile similar to a Ford Focus that has a business basis of \$15,300 is driven 15,000 miles a year for 5 years and then is sold**
3. **Operating expenses include:** maintenance (including car washes), repairs, tires, gas and oil, insurance, license fees and registration fees
4. IRS mileage rates do not include interest on vehicle loans (consider amending the past 3 years)
5. **Consider switching from IRS mileage rates to the actual depreciation and operating expenses on your vehicle**
6. **Luxury automobiles** (Business basis of \$15,300 or more) are subject to depreciation limitations (2011 - \$3,060/\$4,900/\$2,950/\$1,775 ...) **Note: year one is for half a year (first year depreciation on “new” luxury automobiles purchased in 2011 increased by \$8,000 of bonus depreciation to \$11,060 from \$3,060)**
7. Purchasing or leasing an automobile are subject to the same documentation rules
8. Under \$75 no receipt required

**Bonus Depreciation Extended by: Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, signed December 17, 2010**

*Notes and Questions:*

# Tax Strategy

## Buy New or Used Section 179 Vehicles

1. Automobiles are subject to depreciation limits
2. Tax defined trucks and vans can qualify for Section 179 expensing and a 5-year depreciable life
3. **SUVs and crossover vehicles** qualify for a special Section 179 depreciation deduction of up to \$25,000 **if the vehicle has a Gross Vehicle Weight Rating (GVWR) of over 6,000 pounds**
4. **Example:** Purchase a **Used \$50,000** qualifying vehicle (100% business use) before October 1 this year and you can deduct **\$30,000** (\$25,000 plus \$5,000 depreciation), October 1 to end of year you can deduct **\$26,250**, assuming over 40% of qualifying equipment was purchased in the last quarter (\$25,000 plus \$1,250 depreciation)
5. **New** qualifying SUVs and similar vehicles purchased in 2011 qualify for 50% bonus depreciation
6. **Example:** Purchase a **New \$50,000** qualifying vehicle (100% business use) before October 1, 2011 and deduct **\$40,000** (\$25,000 plus \$12,500 bonus depreciation plus \$2,500 regular depreciation), October 1 to end of year you can deduct **\$38,125**, assuming over 40% of qualifying equipment was purchased in the last quarter (\$25,000 plus \$12,500 bonus depreciation plus \$625 regular depreciation)
7. The total cost of the property to be expensed for any tax year cannot exceed the total amount of taxable income derived from the business activity (carryover allowed)
8. **Vehicles are not required to be on a “truck” chassis for Section 179. The truck chassis only applies to trucks that are exempted from the \$25,000 SUV limitation and the 6,001 lb. GVWR requirement.**

Business income includes W-2 and other earned income, both yours and your spouse's: IRS Publication 946, *How to Depreciate Property* (2010), page 20

*Notes and Questions:*

# Tax Strategy

## Hire Spouse to Deduct 100% of Medical as a Business Expense When You Do Not Have Employees

1. **Medical Reimbursement Plan can be the sole compensation (IRS approves)**
2. **Deductible by the employer not income to the employee** (eliminates 7.5% of AGI limitation)
3. Must keep track of hours worked and business activities performed
4. Deduct on IRS Form 1040, Schedule C, Line 14, Employee Benefit Programs
5. Individual or Family Plan
6. Covers insurance (health, dental, Medicare, long-term care), OTC drugs, and all other qualified medical (IRS Publication 502, Medical and Dental Expenses)
7. If single, consider a no hassle spouse (C Corporation - you are the employee) or deduct 100% of your health insurance premiums as a front-of-the-form 1040 deduction
8. S Corporations and Partnerships have different rules

Medical as compensation: IRC Section 162(a)(1); Reg. Section 1.162-10(a)

Tax free fringe benefit: IRC Section 213

Your spouse as an employee: IRS Industry Specialized Program Settlement Guideline for Health Insurance Deductibility for Self-Employed Individuals (UIL No. 162.35-02)

Factual issue, January 25, 2001

*Notes and Questions:*