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Ken Berry, JD • Nov. 06, 2014

Do you have clients that began a business out of a spare bedroom, garage or basement? These entrepreneurs may start off as self-employed individuals, selling their wares on eBay or etsy or at flea markets. In some cases, a humble beginning can mushroom into an international conglomerate.

The ranks of the self-employed keep swelling. According to the Bureau of Economic Analysis of the U.S. Department of Commerce, 99 percent of the employment increase from 2000 to 2011 occurred in the self-employed sector. In comparison, self-

profit from your self-employed business, as well as state income tax in all but seven jurisdictions (Alaska, Florida, Nevada, South Dakota, Texas, Washington and Wyoming). But the taxable amount isn't just the difference between the amount charged and the cost of good sold or services provided. By maximizing deductions, where warranted, you can reduce the amount subject to tax for both federal and state income tax purposes.

2. **Self-employment tax:** This is the equivalent of the Social Security and Medicare tax that a corporate employee has to pay. Because the employer is normally responsible for its share of these taxes, you're effectively paying twice the amount of tax an employee does. For 2014, the self-employment tax is equal to 15.3% on income up to $117,000 (increasing to $118,500 in 2015) and 2.9% on amounts above that threshold. Saving grace: You can deduct half of the self-employment tax you pay "above the line" on your Form 1040.
3. **Other employment tax:** The tax bucks don't stop there. If you employ workers beside yourself, you must pay half of their Social Security and Medicare taxes, plus unemployment tax and, in some cases, temporary disability tax, to the proper authorities. In addition, you're responsible for withholding the requisite employment taxes and depositing those amounts with the IRS. Clients often disregard or ignore these rules with painful results. Under the "100% penalty," a business owner may be held personally liable for underpayments if they are due to willful failure. Advise clients to pay the IRS first.
4. **Sales and use taxes:** This is a lightening rod for controversy among online sellers. Generally, a state will impose its own state sales tax, so you're bound by the applicable laws of the state of where your tax home is located, at a bare minimum. But you're also responsible for collecting sales tax from buyers in a state where your business maintains a physical presence. You will have to investigate the laws in each of those states to find out the procedures for registering and paying over the proper amount of tax. Note that the rules can vary widely from state to state

(e.g., goods that are excluded from sales tax in one state might be subject to tax in

Agreement (SSUTA), a consortium of 46 states and the District of Columbia have joined together to simplify sales tax collections for sellers across a multitude of states. Currently, compliance is voluntary for online sellers, but the SSUTA is often cited as a linchpin for proposed federal legislation.

Keep your self-employed clients apprised of their obligations under existing law as well as new developments that could affect them in the future. Contact them now before they call you in a panic.

Sales Tax • Taxes