

An Overview of Tax Filing Requirements for Real Estate Broker/Agents



HOBERTMAN & LESSER, LLP
Certified Public Accountants & Advisors



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- A two-partner, 25 person firm with 80 years history servicing clients in the areas of: real estate, auditing, accounting, tax, valuation services, government agency services, and management advisory services.
- Clients represent a broad cross-section of businesses and individuals ranging from publically and privately held companies to high net worth entrepreneurs.

Presentation Topics

- Income Tax Filing Classifications
- Form of Ownership
- Self Employment Taxes
- Federal Tax Withholding and Tax Deposits Requirements
- Workers Compensation—NYS
- Home Office Rules for Self Employed Persons
- Unincorporated Business Tax— “UBT”
- Pension Deductibility and Retirement Planning
- Health insurance



Income Tax Filing Classifications — Individual, Partnership, LLC, S Corp

Self Employed—Earnings

Generally, Real Estate Agents receive payment in the form of commissions. The filing status for a real estate agent is generally a “self-employed individual.” (TRC Section 3508 treats a qualified real estate agent not as an employee of the broker—to achieve this status, services performed are pursuant to a written contract)

- All earnings related to real estate sales must be reported to the Internal Revenue Service (IRS) on your personal Income Tax Return, Form 1040, Schedule C.*
- Earnings include all compensation on Form 1099 that an agent receives from his broker, plus any additional income whether it is reported on a 1099 or not.

* This would include a single member LLC entity, which is a “Disregarded Entity” by definition.



Income Tax Deductions

Deductions—The IRS allows real estate agents to take specific deductions to decrease their taxable income. The most common deductions include:

- Vehicle expenses
- Mileage & local transportation expenses
- Advertising expenses
- Accounting fees
- License fees
- Education costs
- Wages
- Professional dues, educational materials, etc.



Income Tax Filing Classifications – Individual, Partnership, LLC, S Corp

Partnerships/LLC's

- A partnership must file an annual information return to report the income, deductions, gains, losses, etc., from its operations, but it does not pay income tax. Instead, it “passes through” any profits or losses to its partners. Each partner includes his or her share of the partnership’s income or loss on his or her tax return.
- Partners are not employees and should not be issued a Form W-2. The partnership must furnish copies of Schedule K-1 (Form 1065) to the partners.
- Partnership tax returns are less likely to be audited than Schedule C’s.



Income Tax Filing Classifications – Individual, Partnership, LLC, S Corp

S Corporations

- S corporations are corporations that elect to pass corporate income, losses, deductions and credit through to their shareholders for federal tax purposes. Shareholders of S corporations report the flow-through of income and losses on their personal tax returns and are assessed tax at their individual income tax rates. This allows S corporations to avoid double taxation on the corporate income.
- In order to become an S corporation, the corporation must submit Federal Form 2553 Election by a Small Business Corporation (and the corresponding State election form), signed by all the shareholders.



Supporting Documentation

Documentation*

- For eligible tax deductions, the IRS requires real estate agents to have proper documentation.
- This includes receipts for deductible expenses such as vehicle repair and insurance.
- For travel mileage, the IRS requires keeping a daily log showing the date, starting mileage and ending mileage for each work day.

* These rules apply to individuals, partnerships and corporate form of ownership



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Estimates

Estimated Tax Payments

- Paying estimated taxes is required if a real estate agent owes more than \$1,000 in taxes at the end of the tax year.

Payment Due Dates for the tax year 2013

- You can pay all of your estimated tax by April 17, 2013 or pay the Estimated Tax in four equal amounts by the following dates:
- 1st payment April 17, 2013 *
- 2nd payment June 15, 2013 *
- 3rd payment Sept. 17, 2013
- 4th payment Jan. 15, 2014

* Attention to the first two estimated payments is necessary to avoid penalties for underpayment for the year.



Estimated Income Tax

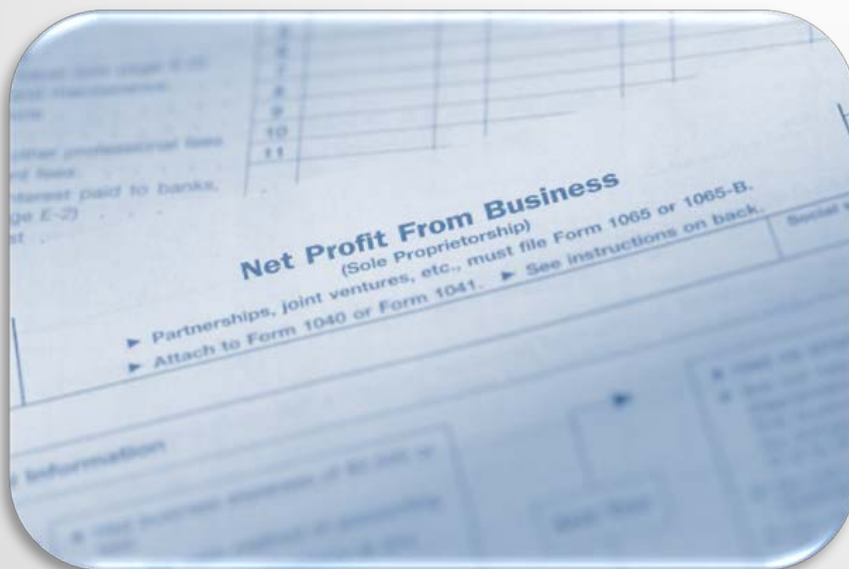
- Payments by mail must be postmarked by the estimated tax due date.
- The date of the U.S. postmark is considered the payment date.
- Payments may be made electronically.
- You may be charged a penalty if you don't make the required quarterly payment amount through withholding or estimated tax payments.



Income Tax

How Do I File My Annual Return? (Self Employed)

- To properly file your annual tax return, you must complete Schedule C to report your income or loss from the business you operated.
- The Schedule C Form is a part of the individual 1040 Tax Return filing.



Self Employment Taxes (SE)

- As a self employed individual, you are required to pay self-employment taxes, which for 2012 was 13.3 % and for 2013 is 15.3%.
- The SE tax is comprised of 10.4% for Social Security and 2.9% for Medicare for 2012. In 2013 the Social Security component increases to 12.4% so the SE tax will be 15.3%
- Only the first \$110,100 in 2012 and \$113,700 for 2013 of self employment earnings are subject to the Social Security portion, but all self employment earnings are subject to the Medicare tax.



Self Employment Taxes

Deduction for Self Employment

- You can deduct half of your SE tax in figuring your Adjusted Gross Income.
- It does not affect either your net earnings from self-employment or your SE tax.



Federal Tax Withholding and Tax Deposits – Employees of Self Employed

W-4 Employee's Withholding Allowance Certificate

- Employee(s) must complete form W-4 and NYS IT 2104, Employers Withholding Allowance certificate, for the employer so that you withhold Federal, NYC, and NYS taxes at the appropriate rates.

Other Forms Required from your Employees

- When hiring an employee an I-9, Employment Eligibility Verification must be completed by the employee to document that the new employee (both citizen and non-citizen) is authorized to work in the United States.



Federal Tax Withholding and Tax Deposits – Employees of Self Employed

Payments of withholding taxes

- Federal and state withholdings have a frequency of payment schedule based upon the amount withheld.
- Income and Social Security taxes are required to be withheld from payments made to employees. Wages include regular pay, bonuses, commissions, and vacation payments.
- The amount withheld is paid to the IRS and the state tax department in the employee's name.



Federal Tax Withholding and Tax Deposits – Employees of Self Employed

- Taxpayers must deposit all Federal depository taxes (such as employment tax, excise tax, and corporate income tax) electronically using the Electronic Federal Tax Payment System (EFTPS).
- The timing of deposits are based upon the amount of tax withheld by the employer for all employees.



Federal Tax Withholding and Tax Deposits – Employees of Self Employed

Depositing Employment Taxes

- Penalties are assessed if deposits are not paid timely
 - 2% - Deposits made 1 to 5 days late to
 - 15% - Amounts still unpaid more than 10 days.
Similar Penalties apply to State Tax withholding.
- Withholding Taxes are Trust Taxes that become a personal liability of the **responsible individuals** and if not paid to the taxing authorities will be subject to a 100% penalty that is imposed on the responsible individuals, plus the unpaid Trust Taxes.



Federal Tax Withholding and Tax Deposits – Employees of Self Employed

Reporting Employment Tax— Employer's Quarterly Federal Tax Return (941)

- The Employer is required to file Form 941 Quarterly. It is the accumulation of employee wages, withholdings, and payments of taxes during the quarter.
- An equivalent form is filed for state and city tax purposes.
- Year end figures are reported on a W-2 for Federal/State purpose.



Federal Tax Withholding and Tax Deposits – Employees of Self Employed

Social Security and Medicare Taxes

- In addition to the withheld Social Security and Medicare taxes from your employees' wages, the employer is required to pay a matching amount.
- Therefore, for 2012 the tax is comprised of 4.2% for social security and 1.45% for Medicare withheld from the employee and a 6.2% and 1.45% match by the employer for a total tax rate of 13.3%. For 2013 the total is 15.3%.



Federal Tax Withholding and Tax Deposits – Employees of Self Employed

Federal Unemployment Tax Act (FUTA) and State (SUTA)

- Pay FUTA/SUTA tax separately from Federal Income tax, and Social Security and Medicare taxes.
- The employer pays this tax. Employees do not pay this tax or have it withheld from their pay.



Workers Compensation – NYS

Complying with the Law—NYS

- The Workers' Compensation Law requires that employers obtain and continuously keep in effect workers' compensation coverage for all their employees.
- Penalties for failing to properly comply are onerous.

Businesses meet this requirement of the law by:

- Obtaining and maintaining a workers' compensation insurance policy; or obtaining self-insurance for workers' compensation.



Workers Compensation – NYS

Posting of Notice of Workers' Compensation Coverage

- According to Section 51 of the Workers' Compensation Law, employers must post a Form Notice of Compliance–Workers' Compensation law (C-105). Most employers obtain this form from their workers' compensation insurance carrier.
- The Workers' Compensation Board prescribes Form C-105 and requires that the form include the name, address and phone number of the insurer and the policy number of the employer. It must be posted in a conspicuous place in the employer's place of business. Violations of this requirement can result in a fine of up to \$250 per violation.



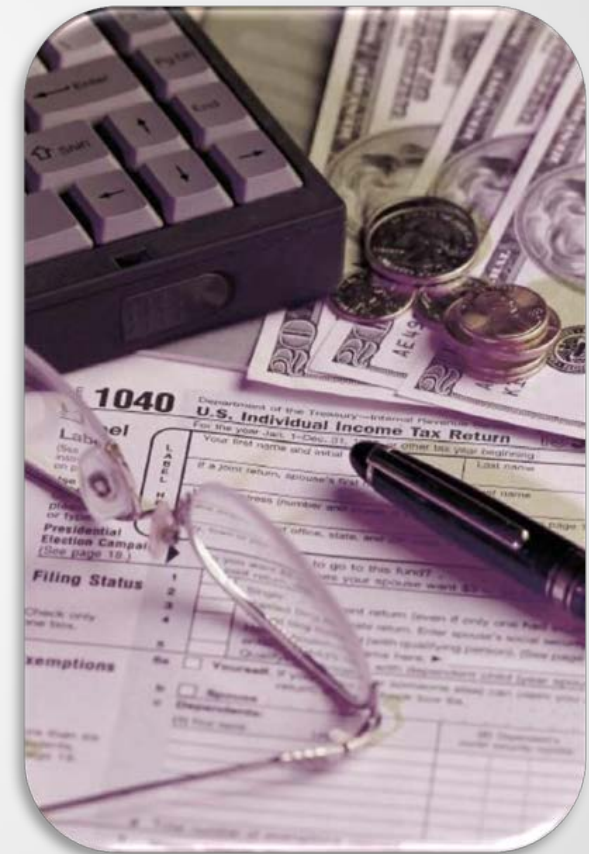
Home Office Rules for Self-Employed Persons

- A self-employed taxpayer reports income and expenses attributable to the business use of his home on Form 1040, Schedule C, Profit or Loss from Business or alternatively on Forms 1065/1120S if a Partnership or S Corporation.
- The self-employed taxpayer must also attach the following forms to his/her return: Form 8829, Expenses for Business Use of Your Home, and Form 4562, Depreciation and Amortization, if he/she claims any depreciation allocable to the business use of his home.



Home Office Rules for Self-Employed Persons

- Note that part of otherwise personal deductible expenses — e.g., taxes and interest allocable to the business use of the home—are reported on Schedule C, but the balance of such expenses may be claimed as an itemized deduction on Schedule A to Form 1040.



Home Office Rules for Self-Employed Persons

Sale of Your Personal Residence – Capital Gains Exclusion

- If you are married and file a joint tax return, you may be able to exclude up to \$500,000 of gain on the sale of your personal residence. If you are single or married and filing a separate return you may be eligible to exclude up to \$250,000 on your return.
- If you use a portion of your home for business purposes, the portion of the home used for such purpose will not qualify for Exclusion on the gain on a sale if the property is sold, since it has been converted to Business and not Personal use.



Unincorporated Business Tax (UBT)

New York City imposes a tax on every individual or unincorporated entity carrying on a trade, business, or profession – in whole or part effective tax years beginning 2009 .

Who must file a UBT tax return?

- Individual or unincorporated entity that has **gross receipts** greater than \$95,000.
- Who must ultimately pay the 4% UBT tax—any person whose **net self employment earnings** from NYC are \$100,000 or less receives a UBT tax credit which offsets the UBT tax in full and results in no UBT tax due, but must file the UBT Form.



Unincorporated Business Tax (UBT)

Who must file a UBT tax return? (continued)

- A gradually phased out partial UBT tax credit is available for persons whose **net self employment earnings** from NYC are greater than \$100,000 but less than \$150,000.
- Any person who has **net self employment earnings** from NYC greater than \$150,000 must pay the UBT tax and will have no credit to offset their UBT liability.



Unincorporated Business Tax (UBT)

- The chart (hand out) illustrates numerous gross income and net income from NYC self employment earnings scenarios and shows whether that scenario results in a filing requirement or tax due.
- A credit for NYC UBT Tax paid is available to offset NYC income tax on a resident or part year resident tax return.
- The credit is equal to 23% or more of the UBT tax paid.

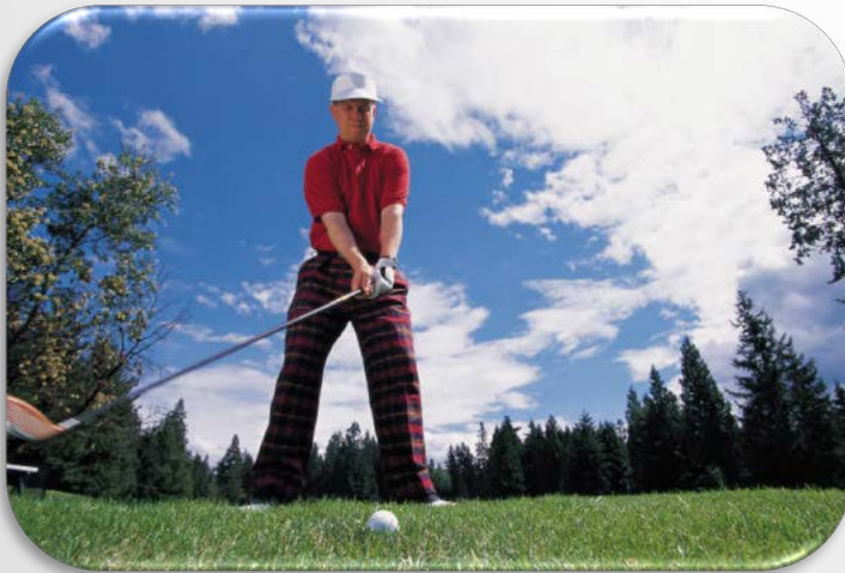


Pensions

Retirements Plans for the Self Employed

Some types of retirement-savings options are:

- Simplified Employee Pension (SEP)
- A solo 401(k) plan
- IRA – Individual Retirement Account (Traditional and Roth IRAs)



Pensions

Retirements Plans for the Self Employed

Some considerations for retirement-savings options are:

- Contributions are tax-deductible and grow tax-deferred until you withdraw the money in retirement.
- With a SEP, you can contribute up to 20% of your net self-employment income up to a maximum of \$50,000 for 2012 and \$51,000 for 2013.



Pensions

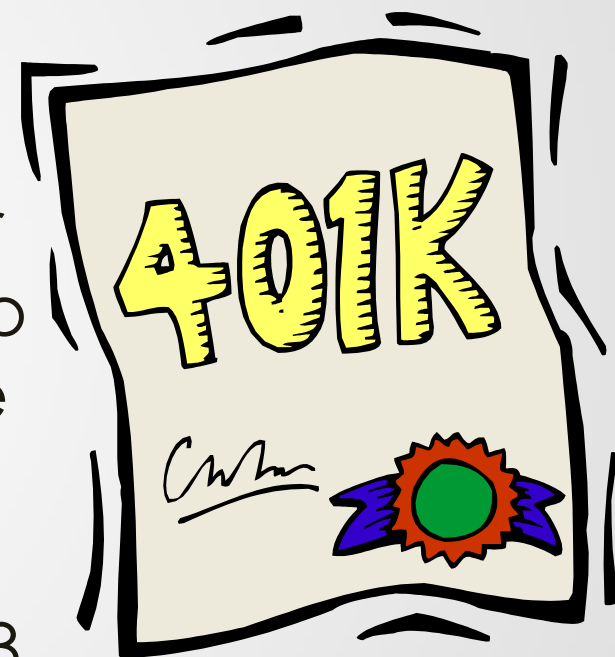
Example:

- Net self employment income = \$107,124 less one half of self employment tax of \$7,124.
- Maximum Contribution is \$20,000 ($\$107,124 - \$7,124 = \$100,000 \times 20\%$)
- Maximum contribution can be achieved at \$250,000 of net Self Employment income (\$50,000)



Pensions

- A solo 401 (k) has the same maximum contribution limits as an SEP, except that you are allowed to make additional contributions.
- You can contribute up to 20% of your net self-employment income to a solo 401 (k) *plus* up to \$17,000 in employee salary deferral for a maximum contribution of \$67,000 for 2012 and \$68,500 (\$17,500 plus \$51,000) for 2013.



Pensions – Example

- Net self employment income = \$107,124, less one half of self employment tax of \$7,124.
- Maximum Contribution is \$20,000 ($\$107,124 - \$7,124 = \$100,000 \times 20\%$)
- Add: Employee Maximum Salary Deferral of \$17,000
- Total Solo 401 (k) contribution is \$37,000 (\$17,000 plus \$20,000)
- Maximum contribution can be achieved at \$250,000 of net Self Employment income (\$50,000) plus \$17,000 of Maximum Salary Deferral.



Pension Contributions

- And if you are 50 or older by the end of the year, you can make catch-up contributions to a solo 401(k)—but not to a SEP—of up to \$5,500, for a maximum contribution of \$55,500 in 2012.
- For 2013, the maximum you can contribute to all of your Traditional and Roth IRAs is the smaller of \$5,500 (\$6,500 if you're age 50 or older), or 100% of your taxable compensation for the year.



Self Employed-Health Insurance

A deduction for health insurance expenses for yourself, your spouse, and your dependents may be taken if you have self-employed income (but it cannot create a loss).

Maximum Limit for the Self-Employed Health Insurance Deduction

- Before claiming a tax deduction, you must calculate your allowable health insurance deduction.
- Take your self-employment net income before the deduction for self-employment taxes, subtract any retirement contributions you make to SEP-IRA and the 50% deduction.
- The remainder is your allowable deduction for health insurance expenses.



Self Employed-Health Insurance

Health Insurance Deduction in a Loss Year

- If you are reporting a loss from your self-employed activity, then you are not eligible to deduct your health insurance costs since this particular deduction is limited by your self-employment income, as adjusted.
- You can however claim the health insurance expenses as an itemized medical deduction on Schedule A of your personal tax return.



Our firm is here to assist you with any tax compliance or planning issues that you may have. Please contact Robert Hoberman at 212-463-0900 or email robert@hobermanlesser.com for further information and advice.

We look forward to being a part of your success and appreciate the opportunity to make this presentation.



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