So, you started a party plan business?

Read this article for some important information.

Pampered Chef, Partylite, Home Interiors, Tupperware, Avon, or one of several others - all party plan sales businesses. Easy enough to start, but come tax time, no longer so easy. In this article, I'll give you some basic information about the things you'll need to keep track of so that tax time will be a snap.

The first thing to keep in mind is that a business, be it a corporation like Wal-Mart or General Motors, or your home-based party plan business, is a separate entity. That means that you need to keep your personal income and expenses separate from the business income and expenses. The best way to accomplish this is to establish separate banking and credit accounts for the business. Now, we know that this isn't always practical or cost effective, and one of the benefits of a "sole-proprietorship" over a corporation or a partnership is that this isn't actually required. But you should try and keep as much of the income and expenses transactions for the business separate from personal transactions.

Income

The first thing needed to complete the tax return will be gross income. Gross income includes all income to the business, such as sales, awards received, bonuses, etc., but does not include money loaned to the business by the owners or others. It is important to keep loan transactions separate from income transactions. You don't want to pay taxes on loan money that you have to pay back. Many businesses use cash deposits as a way to determine income, however, this can cause problems by not properly accounting for any loans or other cash deposited that aren't income. The best way to keep track of income is to keep a total of all transactions that include income items like those listed above. It is also important to keep to keep extra collections, such as sales tax and bottle deposits, separate from income as well.

In many party-plan businesses, the income figure is actually the easy part. Many of the party-plan companies send 1099's to their sales people that give the totals of their sales, awards, etc. The hard part is actually tracking the expenses of the business. Most business owners actually *underestimate* their expenses when filing their taxes because they simply don't remember everything they've spent on the business. The simple truth is that most party-plan businesses lose money, but since the bookkeeping is weak, they don't realize it.

Expenses

Expenses include the costs of product sold, utilities such as telephone, office supplies, car expenses, and more. It is very important to keep track of the expenses of the business or you will pay too much tax. No one wants to do that. A general rule of thumb when trying to determine if an expense is a business expense or a personal one is to determine why the purchase is being made. Think to yourself “if I was not in this business, would I still buy this item?” If the answer is no, it sounds like you have a business expense. If the answer is yes, you have a personal expense. You can allocate personal expenses to the business, such as buying a package of file folders and using half for business and half for personal use. In this case, you can deduct half the cost of the file folders since you used half for business.

Expenses on the tax return must be categorized. So keep your records the same way. Categories include things like rent, wages, utilities, advertising, bank fees, taxes and licenses, etc. You can categorize any way that works for you, but you can’t just report a total.

Special rules for expenses

Telephone

Certain expenses have special rules to follow in order to deduct them. One is telephone usage. The first line into a home is not deductible since it is defined as a personal expense. However, with more and more people using cell phones as their primary phone, this rule may change in the future. In the meantime, only itemized calls on the first line can be deducted. Itemized calls are calls such as long distance that are itemized on the bill and a cost can be determined for. The cost of the calls and the associated taxes can be deducted.

Auto Mileage

Auto expenses are another special case. Contrary to what many people think, gas receipts are not generally used or needed for auto deductions. In order to properly deduct auto use, you must track mileage on the vehicle. The first thing needed will be the total number of miles, for all uses, put on the vehicle during the tax year. The easiest way to determine this is take your odometer reading on January 1st of each year. This will give you the total mileage for the year. The second item needed is commuting miles. Commuting miles are the miles you drive back and forth to work, or your primary job, each day. You don’t have to track this exactly. Just knowing the average round trip and the number of days worked during the year will be enough to get the number we need. Lastly, we need the number of business miles driven. This is the money number. It is this number that will determine your deduction, and it is almost always *underestimated*. It is important to keep a log of business miles. A log is the only proof you’ll have of business miles driven. It is best to get into the habit of writing the beginning and ending odometer reading for any business trip made. Keep in mind, business trips can include trips to purchase and drop off goods and supplies, trips to the office supply store, or any other trip made because of business reasons.

Meals and Entertainment

Sometimes, you want to take your clients out for a dinner, or bring snacks to the party. Meals and entertainment expenses are tricky. First, something open to the general public, like the party for the party-plan sales, will be fully deductible. So if you stop and grab appetizers for the group and bring them along, no problem. However, if you take the host out to dinner later on because that party generated your best sales yet, that dinner won't be fully deductible. Meals and entertainment expenses are only 50% deductible, and in order to be deductible at all, the dinner must have a business purpose. You should keep the receipt and document on the receipt the business purpose for the meal and what business was discussed during the meal. This is your backup in case of audit.

Assets

Generally speaking, items purchased for the business such as fax machines, chairs, cabinets, etc., will be written off directly as expenses since the cost is small. A rule of thumb here is about $300. More expensive asset purchases must be depreciated. Depreciation is a topic a little more advanced than this article, but depreciation is a method to write off the costs of assets over time instead of immediately. The purchase receipt should be on hand at tax return preparation time to be able to ensure the depreciation calculations will be correct.

Office in the home

Office in the home is a tricky deduction. The vast majority of taxpayers with a small business won't qualify for the office in the home deduction. It is a hard deduction to qualify for, and to take. First, the requirements: the area used for the business must be only used for business. If you have a computer room used for business, but you also have a TV in the room, the TV is considered personal and can disqualify the deduction. There doesn't need to be a minimum amount of space, and it doesn't have to be a separate room, but it does have to be 100% business use. Second, the office in the home must be for the convenience of the employer. In the case of a small business, the employer is you, so this one isn't so difficult.

Once the qualification is determined, the difficult part is determining the amount of the deduction. The starting point is the space used for business. We need to determine the percentage of home space used for business. Then this percentage can be applied to your home expenses, such as gas and electric, homeowners insurance, home repairs like roof or furnace, mortgage interest or rent payments, etc. The area of the home is also depreciated, which can cause problems with home gain exclusions down the road when the home is sold. Generally speaking, the amount of the deduction is usually very little and not worth it unless a large area of the home is used.

Bottom Line

Some of the information here may seem a bit intimidating, but don't worry. Some may not apply to you, and once you get into the proper habits, it'll be easy as pie. It's a whole lot easier to start out correctly than to try and recreate it during your tax appointment! Relax, take a breath, and be organized!