TOP ACCOUNTING TIPS FOR YOUR BUSINESS

LANDMARK

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WONDERING ABOUT YOUR BUSINESS' TAXES?

Business Structure Matters

New and potential business owners should take care when selecting their business entity structure. How you and your business will be taxed is wholly dependent on the entity structure you select. Not only do you need to consider both your current **and** future tax outcomes, you also need to ensure that your entity serves the needs of your business partners and investors. Because so much rides on your business entity structure, make sure that you are well informed before you make your selection.

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Legal Vs. Tax Entity

Ideally, taxpayers will consult both a lawyer and an accountant before they select their business entity structure because a business's legal structure will influence its tax structure. In the U.S., most new businesses form as Corporations or as Limited Liability Companies (LLCs) (although Limited Partnerships, Professional Associations and Limited Liability Partnerships are also common legal structures). **Corporations** are taxed either as C corporations or S corporations, and **LLCs** can be taxed as sole proprietorships, partnerships, C corporations or S corporations. To select your ideal legal structure, you should understand the tax implications of all four tax structures.

LEGAL STRUCTURE	TAX STRUCTURE
Corporation	C Corporation, S Corporation
LLC	C Corporation, S Corporation, Partnership, Sole Proprietorship

Sole Proprietorship

The only way that your business can be taxed as a sole proprietorship is if you are the sole owner of your business. You can organize yourself as a single-member LLC with your state, or you can remain unincorporated. Either way, you will report your business's income and expenses on your personal income tax return.

TAX CONSIDERATIONS

Sole proprietorships are not independent entities in the eyes of the IRS. You will report your business's income and expenses alongside any other earned or unearned income that you have. You will report your business information on Schedule C, *Profit or Loss from Business (Sole Proprietorship)*, which will flow to page 1 of your personal tax return (Form 1040). The taxes for sole proprietorships are easy to calculate, but you may miss out on business deductions that you would be eligible for if you filed using any of the other three tax structures.

Partnership

LLCs are not universal legal entities across all 50 states, but most states have a legal structure that provides similar protections and opportunities to its owners. If you organize your business entity structure as an LLC, you and your co-owners will file your taxes as a partnership unless you elect to be taxed as a corporation. If you file as a partnership, there are a few things you should know.

TAX CONSIDERATIONS

Like sole proprietorships, partnership income and expenses will be reported on each owner's individual income tax return. **Unlike** sole proprietorships, the IRS requires partnerships to file a separate tax return for their businesses first. Partnership income and expense should be reported on Form 1065, *U.S. Return of Partnership Income*.

The business's income and deductions as reported on Form 1065 will be divwied up among the partners per the partnership agreement. The allocation does not have to be proportional to each partner's ownership; the partnership agreement can state that Partner A reports 100% of the income and 80% of the expenses while Partner B reports 0% of the income and 20% of the expenses, if that is what the partners agree to. This sort of freedom can be an invaluable part of your tax plan, but you will need a good team of CPAs to help you with the reporting complexities.

C Corporation

If you legally incorporate your business or make a certain election as an LLC, you will file your tax return as a C corporation. C corporations are not a common business entity structure for most new businesses. C corporations are administratively burdensome compared to other tax entities, and founders have less control over the entity as it grows.

TAX CONSIDERATIONS

C corporations are the only tax entities that will report and pay their own taxes. They will report their income on Form 1120, *U.S. Corporation Income Tax Return*. Business owners will only pay taxes on (1) salaries and bonuses that they receive (assuming they are also employees of the business), and (2) dividends they receive as stock owners.

Double taxation can be one of the biggest downsides of C corporations. Double taxation occurs when a business's income first gets taxed by the corporation (on Form 1120) and then by the individuals when they are awarded dividends (on Form 1040).

S Corporation

To avoid double taxation and some of the clerical burdens that come with C corporations, many small business owners elect to be taxed as S corporations instead. For a **corporation** to file their taxes as an S corporation, they must make what is known as an "S election." To make an S election, you and your CPA will file a simple form with the IRS. For an **LLC** to file as an S corporation, they must first check the appropriate box to file as a C corporation, and then immediately make an S election. Both elections are easy to make and very common. The timing of the S election can be a bit tricky, so make sure you talk to your accountant before you begin business operations.

TAX CONSIDERATIONS

S corporations file their business information on Form 1120-S, *U.S. Income Tax Return for an S Corporation*. Just like sole proprietorships and partnerships, S corporations pass business income down to their owners/shareholders. Business income, deductions, gains and losses must flow down to the shareholders in proportion their relative investment. This limitation and a few other operational requirements make S corporations less flexible than partnerships.

Make Your Selection

Settling on one ideal business entity structure is easier said than done. The pros and cons of each may never reveal an obvious “best option.” But your CPA can help you make that determination. Every year, our CPAs guide small businesses through this entity selection process, and we would be happy to help you navigate. Contact us today if you need help.

DON'T FORGET TO REGISTER YOUR BUSINESS

"You don't know what you don't know."

Does this statement ring true to you? Those who are just starting a business often struggle to find the information they need to successfully get their idea off the ground. There are articles out there to help you establish your sales tactics, teach you about manageable growth, and manage your finances, but very few help you take that first step.

If you are concerned that you are missing an important step in starting a business, don't fret; we can help. One of the most commonly overlooked steps in starting a business—and something you should do before you do almost anything else—is to register your business with your state.

State Business Registrations

To operate your business as an entity outside of yourself, you must register it with your state. You can treat state registrations like red tape requirements if you'd like, but we recommend that you look at the process as an opportunity to finally answer the tricky questions that you've been wrestling with. As you go through the registration forms, take a critical eye to your business practices and understand why you are checking certain boxes. If you can feel confident that you checked the right box, you'll be off to a great start.

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SELECTING AN ENTITY TYPE

By registering with your state, you are legally forming your business. This one decision will impact your commercial standing, your financial risk, and your tax position. Since so much of your success rides on this one decision, seek the advice of a lawyer and a CPA to help you make the right choice. Partnerships, LLCs, corporations and nonprofits are all treated differently under the law. Be familiar with your entity's operational parameters, and if more than one person will own the business, create an operating agreement.

CHOOSING AN ENTITY NAME

Your Secretary of State's office will be able to tell you your state's business naming requirements. For example, in Arkansas, every corporation must include the word "Corporation," "Incorporated," or "Company" in its name, or a shortened version of those titles. You should also do a quick search to see if your chosen name is trademarked.

FILING YOUR DOCUMENTS

Each state's registration process is different, but in general to start a business, you will need to do the following:

- **Create Your Articles of Incorporation or Articles of Organization**
  Your Articles of Incorporation/Organization should include your entity's name, address, the number of shares that you are issuing (if you are a corporation), information about your directors or incorporating team, and the business's purpose.
- **Select a Registered Agent**
  Registered agents will represent you in all manners to the state. You can be your own registered agent, but many businesses use commercial agencies that correspond with the State on your behalf.
- **Send Payment**
  You will have to pay a filing fee to register your entity. Most states also require you to pay a fee each year thereafter when you file your entity's Annual Report.

Other Registrations

Registering your business with your state's business administration office is just the first step. From there, you may need to register with other agencies, including some of the following:

INTERNAL REVENUE SERVICE

You need to contact the IRS if you (1) need an Employer Identification Number (EIN); (2) want to apply for tax-exempt status; or (3) elect into S Corporation treatment.

U.S. PATENT AND TRADEMARK OFFICE

Contact the Patent and Trademark Office if you want to trademark your business name, your brand, or your product.

BUSINESS LICENSES

Your industry or occupation may require you to get a license before you can open for business. Contractors will need to obtain a contractor's license; a liquor store will need acquire a liquor license; a hair stylist will need a cosmetology license; etc.

STATE SALES TAX ADMINISTRATION

Evaluate your state's sales tax applicability and determine if you will need to register and begin collecting sales taxes. Even if you're not required to collect sales taxes, you may be liable for use taxes. You may need to register in more than one state.

STATE PAYROLL AUTHORITY

If you hire employees, you will also need to register for payroll tax. Your payroll tax administration will let you know how frequently you need to file returns and remit payroll taxes.

CITY BUSINESS LICENSES

Your local government may require specific permits and licenses with each municipality having its own unique regulations. This includes things like a building permit, alarm permit, zoning permit or a signage permit.

Next Steps

Starting a business is intimidating, and that's why so many people give up before they even begin. The great news is that each day, you know more than you did the day before. And Arkansas has many resources like the Arkansas Small Business and Technology Center, Startup Junkie, Arkansas Regional Innovation Hub, Dream It Do It and the Arkansas Small Business Association to help you with the guidance you need.

Keep researching, reach out to your networks and build a team of advisors you trust. If you'd like a Landmark CPA on your team or a professional to double check that you've done everything correctly while you are starting a business, contact us today.

SET UP INTERNAL CONTROLS

Successful businesses thrive on good processes.

Internal controls are the processes, policies and procedures that organizations rely on to ensure that financial reporting is accurate, operations are conducted in a manner that is efficient and in compliance with applicable laws and regulations, and assets are safeguarded against theft or misuse. A well-designed and implemented system of internal controls allows management to stay focused on operational and financial performance goals and objectives, without the distractions of unexpected errors, inefficiencies, and surprises. The nature and type of internal controls will look different for every organization, but internal controls should serve one common purpose: **to create an environment that promotes sound business practices, reliable financial reporting, and efficient operations, allowing for effective management of changes in economic and competitive environments, changes in leadership and priorities, and changes in business practices.** When business practices are based on sound controls, organizations are able to operate efficiently and grow quickly.

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Every Organization Needs Internal Controls – Even Small Ones

It can be easy for new business owners to overlook controls when just starting out. Some think they don't have enough employees to perform proper checks and balances, and others just don't know where to begin. A system of internal controls at a small business does not have to be as robust as that of a Fortune 500 company, but understanding the importance of internal controls and building them into business practices is critical to the success of any business. Keep in mind that internal controls are also for the benefit of shareholders, investors, creditors, employees, vendors and customers.

Categories of Controls

Because companies differ, so will their internal controls, but all entities' controls will fit into one of the following three categories.

PREVENTIVE CONTROLS STOP MISTAKES OR FRAUD FROM OCCURRING.

A simple example of a preventive control is a password. By requiring your users to log in, you are **preventing** a non-authorized person from accessing your sensitive information.

DETECTIVE CONTROLS FIND ERRORS OR ABNORMALITIES AFTER THEY HAVE OCCURRED.

Inventory counts and bank reconciliations are examples of detective controls. The purpose of inventory counts and monthly bank reconciliations is to find mistakes that have already occurred. If a physical inventory count is off from what is on the books, or if the bank statement can't be reconciled to the books, you know to dig further into the problem to see what went wrong. The simple process of reviewing activity on the bank statements for unusual activity is a very important, yet simple, detective control that every business owner should do to detect unauthorized transactions.

CORRECTIVE CONTROLS HELP CORRECT MISTAKES ONCE THEY ARE KNOWN.

Data backups can restore data that was lost or corrupted; insurance can help replace stolen or damaged items; and firing an employee who mismanaged company assets can remove the threat of future errors. These are all examples of controls that correct a problem once it has been detected.

When used together, these three categories of controls will promote a healthy and robust control environment.

Assess Your Risk First

Internal controls will never be perfect; the risk of human error, in particular, can never be fully mitigated. Instead, the system of internal controls should create **reasonable** assurance that an organization's financial reports are reliable and operational objectives are met, within the confines of laws and regulations. The first step to developing a system of appropriate internal controls for any business is a comprehensive risk assessment. What could go wrong, and how would it get caught? Ask yourself some of these questions:

- **What information must be safeguarded, and what avenues are there to access that information?**
- **Where is there opportunity for human error or fraud? Do we rely too heavily on one individual for critical processes?**
- **Where in our processes do we rely on judgement?**
- **What are our main objectives, and what mistakes could be made that would prevent us from meeting those objectives?**
- **If one of our systems breaks down, will we be able to continue business while it is being repaired?**

Although this is not a comprehensive list of all of the questions that need to be asked, the answers to these and other similar questions will help you design a control environment tailored to the unique aspects of your business. After going through the risk assessment process, you will be prepared to explain to your employees the "why" behind your new policies and procedures. Because, remember...

YOU Are Responsible

A well-controlled environment is impossible to achieve without buy-in from the Board or business owner(s), management, and employees. The members of the Board of Directors or the owner(s) exercise oversight of the system of internal controls; management is responsible for designing and implementing controls to achieve objectives; and employees are tasked with executing those policies and procedures. In the end, a company's system of internal controls communicates values and promotes integrity and ethical business practices to everybody in the organization. As the saying goes, nothing is more important than the "tone at the top."

READ MORE:

How Effective are your Internal Controls

Questions?

Uncertainty and ambiguity surrounding business processes can result in costly mistakes or invite fraud. It is imperative that each company implement processes, policies and procedures that are appropriate based on the nature of the entity and are well designed and implemented. Contact us if you have questions about formalizing your own internal control measures or if you have any other questions about starting a new business. We look forward to hearing from you.

WHY RECORDKEEPING IS IMPORTANT

Recordkeeping – especially good recordkeeping – can be a burden on your time, resources, and patience. But as a business owner, it needs to be one of your highest priorities. When you consistently maintain good records, you're investing in your business's well-being and setting it up for success.

Quality recordkeeping will serve your business in more ways than you may think.

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Recordkeeping Helps You Stay Compliant With the Law.

Your home state, and any others in which you operate, will ask you to keep adequate records in return for the privilege of doing business in their state. Depending on the jurisdiction, they may ask you to provide asset balances, meeting minutes, sales reports, employment records, vehicle logs, inventory information, signed contracts and proof of tax filings. Your bookkeeper and your CPA can help you prepare these items when the time comes, but the ultimate burden will fall to you.

Recordkeeping Helps You File Your Taxes.

Keep your records updated as tax season approaches, yes, but make sure that your records are **detailed**. Your CPA will need both the face of your financials and the line item detail before they can report your information in line with IRS standards. The taxing authorities themselves may also ask for your financial statement detail. If you are audited by the IRS or your state's Department of Revenue (as many new businesses are), you will be expected to prove that your expenses were deductible and that your income was not understated. Having nicely presented balance sheets and income statements are great, but without the detail behind the numbers, they will be much less useful.

Recordkeeping Helps You Monitor the Health of Your Business.

Don't trust your gut, at least not when your business is dependent on it. The only way you can know for certain that your business is doing well is if you have the numbers to prove it. If your books are accurate and up-to-date, you can run reports that show you how your business is progressing. You can compare sales month-to-month to see if you're growing; you can browse through your register to see if any of your expenses are getting out of hand; and with the help of a good accounting software, you can compare your numbers to benchmarks in your industry. For these reports to be accurate, your records must be well-kept, of course, but they must also be current.

How long should you keep your records?

Download our record retention guide now!

Recordkeeping Helps You Acquire Funding.

Banks, lenders, and investors will not provide funding without performing their due diligence. They will ask for proof that your business is successful and stable, and they will want to see that you can competently manage an influx of cash. Most financers will require three to five years' worth of professionally-reviewed or audited financial statements. If you keep good records as you go along, it will be easy to produce the documents that they require. If you're able to receive your funding quickly, you will have the best chance at outpacing your competitors.

Recordkeeping Helps You Utilize Your Time More Effectively.

Don't waste your time in the trenches. If you are furiously entering four months' worth of expenses into your accounting software the night before you pitch your business to a new investor, are you going to be prepared for your meeting? And as your business's leader, is data entry the best use of your time? Keeping on top of your books is key. It may sound counterintuitive to spend a little bit of time each day on maintaining your records, but those small steps will pay off when you need them the most. If you want to further improve your efficiency, hire an accountant to take on the day-to-day bookkeeping tasks. You will feel confident that your books are current, and you can focus instead on expanding your business.

You Get Out What You Put In

The amount of effort you put into recordkeeping will directly correlate with the output that you generate. By investing upfront in maintaining high-quality books, your business will run smoothly in the background, and you can focus on the job you set out to do – run a business.

If you've recently started a business or have plans to get one off the ground soon, contact our CPAs today. And if you need help with recordkeeping, our bookkeepers have many years of experience. We are here to help you succeed.

START YOUR BUSINESS WITH THE END IN MIND

Why Succession Planning Is Important

A comprehensive strategy to get your business up and running should include planning for your own exit. As one of the founders, your departure will have a significant impact on the enterprise itself, your fellow business partners, your customers and your future. So, as counterintuitive as it may seem, how you plan to exit your organization is an important decision to make, even at your business's onset. Take the time to work with a trusted professional to outline your succession plan so that you are prepared for whatever future you encounter.

There are a few questions you should ask yourself as you create your succession plan.

How Quickly Do I Want to Exit the Business?

If you want to make a swift exit from your business, you can sell your assets or equity to a private investor or another business. Although there are times when quick exits make sense strategically, most small business owners hope for a different departure. You want to see your entity succeed even after you're gone, so if you sell to the highest bidder, you lose your ability to influence the company's trajectory and ensure its continued success.

Instead, you can choose to make a slower and more purposeful exit from the business. For instance, if your daughter plans to take over the company when you retire, you can progressively transfer ownership and responsibilities to her over time. By the time you relinquish your last bit of control, she will understand your vision and feel competent in her abilities to carry out your goals.

Your departure will have a significant impact on the enterprise itself, your fellow business partners, your customers and your future.

What Role Do I Want to Play When I Leave the Business?

When it's time to leave the business, do you plan to sell your interests outright and invest in a new opportunity? Or do you hope to retain interest in the business throughout retirement? Depending on the type of entity you form, you may be able to hold onto voting or nonvoting membership interests, even after you've surrendered your operational responsibilities of running the business day to day. Your team of lawyers and CPAs will need to know your exit goals so they can form an entity that can provide you those options.

Who Will Take Over the Business When I Leave?

Choose your successor wisely. Selecting somebody who can competently run the business is important, but selecting somebody who will further your vision for the company is critical. You want somebody who shares your values who you can trust to carry on what you've built.

When first starting a business, some owners believe that their family members will fit that bill. Before making any assumptions, you should first confirm that your family member **wants** to take over the business. Even if they say yes, check in with them often to see if they've changed their minds. Only a willing participant will make a good successor.

How Long Will it Take My Replacement to Learn the Ropes?

On day one you may not immediately know who your replacement will be, and that's ok. Instead, you can create an employee training program to groom key workers to take your place. When the time comes to put that plan into action, start small. Ask your candidate to take over one process at a time so you can see if they are up to the task. As you give them more responsibility, do they remain sharp and driven? Somebody who is not a perfect fit **now** can be groomed to excel as your replacement with the right training program.

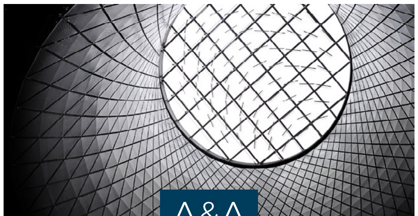
Making a Succession Plan: Practical Steps

Your team of CPAs and lawyers should help you with the following practical aspects of creating a succession plan.

- **Identify key employees that you think would be good candidates to carry on your business and mentor them.**
- **Share your knowledge and experience with your key employees and other members of your management team to ensure that you aren't the only one with all the answers.**
- **Create well-defined career paths and identify the criteria that your employees will need to meet as they grow in their careers with you.**
- **Make sure staff members have skin in the game. You want your key employees to feel motivated to carry on the business with pride.**
- **Make your mission statement for the company public so employees know what your business stands for.**
- **Foster a positive working environment to avoid high turnover or employee complacency.**
- **Keep an eye on industry norms for working hours and promotion timelines. You don't want to lose employees over job dissatisfaction.**
- **Draft a will that details who will control your ownership rights when you pass.**

If you have questions about or want assistance with developing a succession plan, contact us today. We look forward to hearing from you.

OUR SERVICES



A&A

Our teams are trained to search for overlooked trends and identify opportunities specific to your operations.

ACCOUNTING SERVICES

Keeping you on track with personalized, comprehensive solutions including accounts payable/receivable and bookkeeping.

TAXATION

Our tax experts can help you find the right solution for your unique situation.

CONSULTING

Our professionals bring insights to your challenges.

INFORMATION TECHNOLOGY

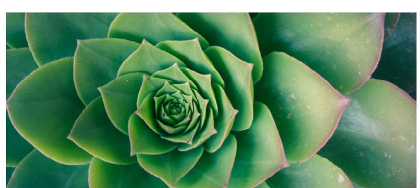
Our IT team can guide you through the technology maze.

FRAUD EXAMINATION

Fraud in the workplace is more common than you think. We can help you mitigate your risks.

BUSINESS VALUATION

Get a clear definition of the value of your business from our specialists.



WEALTH MANAGEMENT

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We look beyond the numbers to provide personalized attention and tailored management assistance.

ABOUT LANDMARK

As one of the **largest locally-owned public accounting firms** in Arkansas, Landmark provides a full range of assurance, advisory, accounting and tax services to a diverse client base. The firm's talented employees offer clients the best of both worlds: the personalized attention and enthusiasm of a local accounting firm combined with the skills, depth of knowledge and breadth of services expected from a national organization.

To set up a **free consultation**, visit our website at https://www.landmarkcpas.com/contact-us/

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