

FAQ's from past COUNSELING

1. What income tax rate does a Sole Proprietor, LLC, Partnership and S Corporation pay? Are there tax advantages of one versus another?

The answer is 'none'. These business entities do not pay income taxes. The net profit or loss is reported by the business owners on their individual income tax Form 1040. Tax returns are required to inform the IRS of each owner's share of the profits which should be taxed to them individually.

The Federal 'Individual' tax rates for "Married" filing joint return for 2010 were:

Income over	Not over	Tax	+ Rate over min
\$ 0	\$ 16,750	-----	+10%
16,750	68,000	\$ 1,675	+15
68,000	137,300	9,363	+25
137,300	209,250	26,688	+28
209,250	373,650	46,834	+33
373,650	-----	101,085	+35

The Minnesota 'Individual tax rates for a joint return for 2010 were:

Income over	Not over	Tax	+ Rate over min
\$ 0	\$ 33,280	-----	+5.35%
33,281	132,220	\$ 1,780	+7.05
132,221	-----	9,718	+7.85

2. As a business owner do I have to pay any taxes during the year?

Yes, because there is no withholding on the net profits of your business during the year. When you are an employee, your employer withholds income, Social Security and Medicare taxes from each pay check. As the year unfolds, you must estimate your profit 'for the year' and pay an estimate on April 15, June 15, Sep. 15 and Jan 15. The estimated amount you pay is your projected income tax based on the tables above, **PLUS**, self employment tax on the same projected net profit.

Self Employment tax is 12.4% for Social Security

2.9 for Medicare

15.3% which is the employers & employees share.

The 15.3% rate is reduced to 13.3% by Congress for 2011 only!

3. Do I have to pay sales taxes to Minnesota?

It depends! It depends upon where the customer is located. It depends on whether you selling tangible personal property or services. It is best to check with the Minnesota Sales Tax department to verify your position. Generally, tangible personal property is taxable – unless specifically excluded like food and clothing. Generally services are not taxable – unless specifically cited in the law like lodging or installation labor of tangible property. Here are the components of Minnesota sales tax you may have to collect:

Minnesota	6.875%
Hennepin County	.150
Minneapolis	.500
Transit Improvement-	.250
Anoka, Hennepin, Dakota	
Ramsey and Washington	
Internet or out of state	.00

4. What does it cost to create a LLC in Minnesota?

The Articles of Organization can be filed online with SOS of Minnesota. The form is only one page and costs \$160. You should also consider creating your LLC Operating Agreement by using a template from www.nolo.com or other resource. The Operating Agreement should;

- a. Set forth the members, their contribution and contribution percentages.
- b. Manager of the LLC
- c. Tax allocation if different from contribution percentages
- d. How a member may withdraw or actions on death
- e. And other provisions that set forth how the LLC will function

5. Is there any advantage of an LLC electing to be taxed as an S Corp?

The net profits of both a LLC and S Corp “pass-through” to the owners. Neither entity pays any income tax itself. One difference and potential advantage is how Self-Employment taxes of 15.3% are assessed. In a LLC structure all of the net profits are considered as salary for Self-Employment taxes (Social Security and Medicare). In an S Corp owners are employees and pay the regular taxes on their salaries. As an employee they pay 7.65% for Social Security and Medical and the S Corporation, as employer, pays a matching 7.65%. Any remaining net profit is “pass-through” to the owners as a distribution on Schedule E of the owners Form 1040. This pass-through portion of a S Corp’s net profit is not subject to the Self-Employment tax. An election to be taxed as a corporation is made on Form 8832 and lasts for 60 months.

6. Does Minnesota assess an annual fee for S Corp, partnerships, LLC’s?

The answer depends on how large the sales, property values and salaries are of the entity. Minnesota uses three factors to accumulate qualifying values. These are: 78% of sales, 11% of property values and 11% of salaries paid. If the sum of these three factors is less than \$500,000 then there is no fee. For sums between \$500,000 to \$999,000 the fee is \$100. See MN web for larger sums. If the sum is over \$20,000,000 the annual fee is \$5,000.

7. What is the SIC or NAICS coding system?

The SIC (Standard Industrial Code) is a system of classifying business originally used by government agencies. It has been replaced by the NAICS (North American Industry Classification System) which is a six digit number to identify various business activities. The NAICS is more recent and incorporates many of the online and computer businesses. You will need this number on many business forms and reports. A good source to determine your NAICS is

<http://www.census.gov/eos/www/naics>

8. Is there a resource to compare my business plan ratios with other companies?

Yes, it is called the Risk Management Association statistics, formerly called Robert Morris Associates. These books of 'Financial Ratio Benchmark' statistics are available at most libraries and lending institutions. Each two pages of the books lists 19 financial ratios by one of the 740 industries by Sales or Asset size.

9. How can I conduct market research from home?

Your key to doing market research from home is a free Hennepin County library card. Access www.hclib.org, enter your library card number and you will have access to databases such as Reference USA, plus many others. You can print 25 records at a time from home or 50 from the library. You can identify listings by NAICS number, size, miles from a zip code, etc. The library suggests these databases:

List of Residential listings – Reference USA. Provides number in household, Census income and home valuations, addresses, etc.

List of companies by sales, NAICS, location, etc:

Reference USA – 14 million U.S. businesses

D&B Million Dollar Directory – 2.2 million records of companies with at least 20 employees and \$1 million in sales. Includes executive biographies and key decision-makers. Good for marketing data.

In depth information or magazine articles on a particular large company

Business and Company Resource Center – 450,000 listings

Business Source Premier – 7,400 journals.

Industry surveys

Standard & Poor's – click on Industries

Business & Company Resource Center – Click on Industry

10. Must an LLC "qualify" to do business outside their home state?

It depends! If you engage in 'intrastate' business, i.e., if you have a warehouse in that state and ship to customers within that state – then you must register. If you only engage in 'interstate' business (you sell & ship from your home state to any other state) then you do not have to register. These types of businesses never

have to qualify – mail order, telephone order, website orders, national advertising offers and selling through independent contractors.

“Qualification” is simply a registration process and paying fees. If in doubt, play it safe and check with your attorney.

11. Should an LLC have an operating agreement between members?

Yes, this agreement is similar to a partnership agreement. It should cover classification for taxes; capital contribution of cash, property or services, their value and the percentage interest in the LLC; member withdrawal or LLC liquidation; officers (members or non-members, compensated or not); restrictions on transfer; etc. There are separate template agreements for a one member, multi-member and non-member managed LLC's

12. Can you point me to some basic education on franchising?

<http://www.sba.gov/services/training/onlinecourses/index.html> is a joint presentation by SBA and Frannet on Franchising. Audio presentation <http://www.mnsbao.com/PDFs/IntroFranchising.pdf> is a document by Andrew C. Selden, Third Edition, January 2008

Talk to a local franchising consultant for free. <http://www.frannet.com>, enter your zip code and you will be directed to your closest consultant.

13. Will add others as clients' questions suggest a new repetitive issue.