Business Expenses
And The S Corporation -
What You Really Need To Know!

Presented by:
National Society of Accountants
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Learning Objectives

• Identify Business Expenses Unique to S-Corporations
• Determine Reporting Requirements of Certain S-Corp Expenses
• Assess the Implications of Fringe Benefits and Officer Compensation
S Corporation Expenses

• Intro to S-Corps
  – Popularity
  – Brief History
  – Form 1120S, Schedule K-1
  – Taxes
S Corporation Expenses

• Accounting Methods
  – Cash, Accrual ????
  – §446(a); Rev Ruling 68-35
  – Form 3115

• Overview of Income
  – Trade or Business
  – Other
S Corporation Expenses

• Form 1125-A
  – COGS;
  – Section 263A rules and limitations
    • Under $1 million – No
  – Inventory
Form 1125-A

Cost of Goods Sold

Attach to Form 1120, 1120-C, 1120-F, 1120-S, 1065, or 1065-B.


<table>
<thead>
<tr>
<th>Name</th>
<th>Employer identification number</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>00-00000000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>CORPS R US</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Inventory at beginning of year</td>
<td>1</td>
</tr>
<tr>
<td>2 Purchases</td>
<td>2</td>
</tr>
<tr>
<td>3 Cost of labor</td>
<td>3</td>
</tr>
<tr>
<td>4 Additional section 263A costs (attach schedule)</td>
<td>4</td>
</tr>
<tr>
<td>5 Other costs (attach schedule)</td>
<td>5</td>
</tr>
<tr>
<td>6 Total. Add lines 1 through 5</td>
<td>6</td>
</tr>
<tr>
<td>7 Inventory at end of year</td>
<td>7</td>
</tr>
<tr>
<td>8 Cost of goods sold. Subtract line 7 from line 6. Enter here and on Form 1120, page 1, line 2 or the appropriate line of your tax return (see instructions).</td>
<td>8</td>
</tr>
</tbody>
</table>

9 a Check all methods used for valuing closing inventory:
   (i) Cost
   (ii) Lower of cost or market
   (iii) Other (Specify method used and attach explanation)...

b Check if there was a writedown of subnormal goods.

 c Check if the LIFO inventory method was adopted this tax year for any goods (if checked, attach Form 970). 

d If the LIFO inventory method was used for this tax year, enter amount of closing inventory computed under LIFO.

 e If property is produced or acquired for resale, do the rules of section 263A apply to the entity (see instructions)?
   Yes [ ] No [X] 

 f Was there any change in determining quantities, cost, or valuations between opening and closing inventory? If “Yes,” attach explanation.
   Yes [ ] No [X] 

BAA For Paperwork Reduction Act Notice, see instructions.
S Corporation Expenses

• Line 7: Compensation of Officers
  – The new Form 1125E
  – Determining what is reasonable
  – Supporting what is reasonable
  – Noncash compensation
  – Compensation mistakes

• Line 8: Salaries and Wages
Form 1125-E

Compensation of Officers

- Attach to Form 1120, 1120-C, 1120-F, 1120-REIT, 1120-RIC, or 1120S.
- Information about Form 1125-E and its separate instructions is at www.irs.gov/form1125e.

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Note. Complete Form 1125-E only if total receipts are $500,000 or more. See instructions for definition of total receipts.

<table>
<thead>
<tr>
<th>1</th>
<th>(a) Name of officer</th>
<th>(b) Social security number</th>
<th>(c) Percent of time devoted to business</th>
<th>(d) Common</th>
<th>(e) Preferred</th>
<th>(f) Amount of compensation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>DRAHMA QUEENE</td>
<td>012-34-5678</td>
<td>100 %</td>
<td>25.00 %</td>
<td>%</td>
<td>105,000.</td>
</tr>
<tr>
<td></td>
<td>MAJOR PAINE</td>
<td></td>
<td>100 %</td>
<td>75.00 %</td>
<td>%</td>
<td>100,000.</td>
</tr>
</tbody>
</table>
S Corporation Expenses

• Line 9: Repairs & Maintenance
  – Capitalization rules
• Line 10: Bad Debt
  – Cash basis
  – Nonbusiness bad debt
• Line 11: Rents
  – Real or personal property
  – Self Rental Rules!
S Corporation Expenses

• Line 12: Tax and Licenses
  – Taxes not included elsewhere
  – Sales tax capitalized

• Line 13: Interest
  – Prepaid interest §461(g)
S Corporation Expenses

• Line 14: Depreciation
  – Section 179 – not so fast!
• Line 15: Depletion
  – Property by property basis at the shareholder level
• Line 16: Advertising
S Corporation Expenses

• Line 17: Pension, Profit Sharing Plans
  – Employer contributions
• Line 18: Employee Benefit Programs
  – Less then 2% Shareholders
  – Group term life insurance
  – Meals and lodging for the employers convenience
S Corporation Expenses

• Fringe benefits / employee benefits
  – More than 2% shareholders
  – Rules of attribution §318
  – Officer life insurance
  – Health insurance premiums
    • HRA – DOL Tech Release 2013-03;
    • DOL HRA FAQs;
    • IRS Notice 2013-54
S Corporation Expenses

• Line 19: Other Deductions
  – Pub 535
  – Startup and organizational
  – Meals and entertainment
  – Gifts / Awards
  – Director fees
S Corporation Expenses

Other Stuff to Remember about S Corps

• Non – deductible expenses
  – Fines and Penalties
  – Golf / Athletic Club dues
  – Political & Lobbying expenses
S Corporation Expenses

Other Stuff to Remember about S Corps
• Pass through deductions
  – Health insurance premiums
  – Charitable contributions
  – §179
  – Investment interest expense (NIIT)
S Corporation Expenses

Other Stuff to Remember about S Corps

• Home Office
  – Yes, you can!
  – Rent paid or 2106

• Expenses paid directly by shareholders
  – Reimbursement policy
  – Capital contribution
So, what you really need to know...

- Develop a process
- Ask the right questions
- Document the answers
- Determine an appropriate outcome
For More Information

National Society of Accountants

More information is available including additional materials at:
Booth in Vendor Hall
Or Table in Lobby
800-966-6679
www.nsacct.org