Andrew: This course is about keeping more and more money in your pocket and keeping Uncle Sam off your back come tax time. The course is led by Kyle Durand who runs a law and accounting practice in Seattle. He's also the founder of taxreceipts.com, which will simplify your taxes with a straightforward system. I'm Andrew Warner. I'll help facilitate and I should also saw that this is not tax or legal advice. You guys should, of course, get your own accounts.

Our goal is here isn't to replace your accountant, but to give you an understanding so you can do your job better and so you can have better, more intelligent conversations with your accountant. This is the big board that we're going to use to lead us through this conversation. Those are the big ideas that you're going to get throughout this program. Kyle, the first question I've got for you is what is this photo and what does it have to do with taxes? Where is this? What's this photo?

Kyle: That's a photo of the master bathroom in one of Saddam Hussein's palaces. That's where I started my entrepreneurial journey in 2006.

Andrew: What were you doing in there, by the way, before we continue with this story. What were you doing in Saddam Hussein's bathroom?

Kyle: I was a JAG in the military and had been in the military for a long time. I had been serving in Iraq for about five months. My office is actually in his master bedroom.

Andrew: When you were in there as a lawyer in the military, you had a vision of what was coming up next. What was that? What were you going to say?

Kyle: It was that it was about time for me to move on from the military to go back to my entrepreneurial roots. I was laying in the tub looking up at the ceiling, thinking about where I was going to go from there and how I was going to get there. As soon as I got back to the United States, I started researching. I wanted to open my own practice. I started researching, raking courses on opening my own practice, taking refreshing courses on business law because that's the route I wanted to take.

Andrew: As an entrepreneur, you probably were, and I know you were because you and I talked before this program started, you were gung ho about getting started and you were about to make a mistake that many people in the audience are likely to make and it would have cost you how much money before you explain the mistake?

Kyle: It could have cost me, at least, $50,000 at this point.

Andrew: It's a series of mistakes entrepreneurs make. I shouldn't say it's just one. Can you tell us what one of those mistakes would have been, if not for your wife, who is a CPA who gave you the guidance that you're going to give to the audience? What's one of those mistakes?

Kyle: That's not setting the business up with the end goal in mind. When my brother came to me after I set up my practice, he had an idea for setting up an IT and hardware consulting business. Like the typical entrepreneur, he just wanted to get out there and start hustling and start bringing in the revenues and start setting up the contacts and contracts. Knowing what I knew with my tax law background, I said, "Wait a minute. Let's take a few steps back. Let's think about where we want to go with this and how to set it up properly." So we set up our corporation and we kept the right records to allow us, when the business really started rolling, to take that money out of the business tax-free.

Andrew: To take the money out of his business tax-free?

Kyle: Yes.

Andrew: You're going to show us how to keep from paying all taxes?

Kyle: Well, it's not all taxes. As you contribute the money, we set it up as an S-corporation. So, we were avoiding all the payroll taxes. We saved ourselves.

Andrew: Payroll taxes are you were taking money out for yourselves out of the business?

Kyle: Right, exactly.

Andrew: OK. All right. The other mistake that you were going to make was not keeping proper records, which we talked about before this program started and that can cost you. As you saw in your own business, it would have cost you tens of thousands of dollars because you would have made simple mistakes. With your brother's business, you were able to save tens of thousands of dollars by thinking about taxes properly within the business structure. What we're going to do is we're going to talk about specifics here. These are the specifics that we're going to get to. The first one is, as you alluded to, the importance of keeping records. Can you tell me about a lobbyist that you did some work with and how that factored into his success?

Kyle: Yes, this lobbyist unfortunately fell prey to one of the most common tax myths that's out there, and I'm sure most of your listeners have heard it, and it's that if I charge everything on my business credit card, then that's a good enough record.

Andrew: You know what, when I saw this, you did a session with Jeremy, our producer, to go over what you're going to talk about, and he showed me these notes, I said, "Really?" I always thought that if I'm using my credit card that I've got a record of all my expenses. That's not enough?

Kyle: No. And it's a huge surprise to the vast majority of entrepreneurs.

Andrew: It's not just entrepreneurs who are used to everything just happening automatically without keeping any records. Every time I got a paper record last year, at least, I'd toss it in the garbage. And you're saying it's not enough, for what? My own personal records or the government's?

Kyle: Right, for the government. To get to the story about the lobbyist, this guy he was doing that, and he had a lot of entertainment and meal expenses, which as a lobbyist you would expect. And, meals and entertainment expenses are one of the things that the IRS looks at very carefully. So he charged all these expenses, tens of thousands of dollars, on his credit card, thinking it would be enough. And he came in my office to hire me when he was audited, and in the audit, I told him that his record wasn't going to be enough and asked him to get the credit card receipts and he didn't have any of them. And, the end result was that the IRS disallowed all of those expenses and charged him penalties and interest on it and his tax bill ended up being well over $80,000 for one year, and all of those would have been legitimate expenses if he had kept receipts with it as well.

Andrew: So you're telling me that, if I buy something, say, I go to the computer store and I buy a new monitor for work. Let's say, I go to Best Buy, which I wouldn't use. I buy the monitor, I have it here to work, and I think "OK, great. I can take the expense on that, right that off my revenues." No, unless I have the receipt, the credit card is not enough, I can't back it up and I can't take the expense? Or, is it that if I'm ever audited I'm going to have to undo it because I can't justify it?

Kyle: That's absolutely the point. You can take any deduction you want, it's just when you're audited you won't be able to substantiate that deduction.

Andrew: I see, so they say "Hey, look, Andrew, I see that you're buying a lot of computers", and I say, "of course, because I'm in the tech industry, I need to record, I need to watch, I need to do all kinds of things, so I bought computers." "Can you prove that you bought it, can you show me the receipts?" "Oh yeah, here are my credit card statements! I've been so good about recording them.", and they're going to go, "This does nothing for you. We're going to consider those expenses not having happened and you still need to pay taxes on it."

Kyle: Right. Well, in that case that the auditor goes, "You went to Best Buy. How do I know you didn't buy DVD's? Where's it say what you bought?" It makes intuitive sense once somebody explains it to you, but most people learn the hard way.

Andrew: At this point, I imagine a lot of people are pausing, pretending that they're going to listen later, but internally are thinking "This is just going to be painful for me, I can't continue to watch." So don't avoid this, keep watching, keep listening, keep reading if you're a transcript person, because, Kyle, what do we do to handle this going forward? I don't want to feel bad about my past, I want to find the solution that's going to be good for the future. Should I bring up this next visual?

Kyle: Yes.

Andrew: Let's do it. What do I do to avoid this, and what should my audience, who's very, very special to me, do to assure that they don't make the same mistake that I've just explained that I've apparently made?

Kyle: Yes, so, it's not too late now. Start immediately. The idea is to collect all those receipts. Every time you get a receipt, make sure to keep it, if it's for a business expense of course. And then, to create a system to organize those receipts. A lot of people put them into file folders or a box or something, but any way you do it, just make sure you're collecting and organizing those receipts. With tax receipts we walk people through a simple system where we collect the receipts, we get them in a digital form, you classify those expenses, and they go into your accounting software and you're done with it. It sounds like a lot of steps but, if you're doing it on an ongoing business, it just becomes part of your routine and it's just a couple minutes a week rather than tens of thousands of dollars later when the IRS comes and audits you.

Andrew: OK. When I am already classifying my expenses, if I buy a computer, I categorize it properly as the right kind of expense in my accounting software I use in Dinero. I am imaging a lot of people in the audience use QuickBooks, whatever it is, we are categorizing it, we are entering it into our software. The step that you want to make sure that we take as a result of this program is we keep the receipt. Now, where shall we keep it? Can I just stuff it in a box and then come back to it later on? Can I stuff if in a tickler folder so at least I have it by month? What I prefer to do is I take a picture of the receipt using one of those iPhone scanner apps. Is that enough? The picture of it?

Kyle: Absolutely.

Andrew: OK.

Kyle: A couple of years ago, the IRS came out with some regs. They authorized electronic records. They would be as good as paper records or hard copies. As long as you have electronic record, some sort of record of that receipt, then you are set.

Andrew: OK. All right. For the audience, Kyle just mentioned this website, taxreceipts.com. This is his site. We are not trying to sell you on anything. I know some people get frustrated when they watch a program and they feel like they are being sold throughout the program. Believe me. I would feel that same kind of frustration. There is frankly nothing as far as I know that they have got to sell on here. It is a new site where they are teaching people about taxes. Are you guys operating like true Internet entrepreneurs? You are going to figure out the real revenue model later on? You just want to get this up and running for now?

Kyle: Absolutely. Our main goal is to get the information out there.

Andrew: Right. Teach, do some good, build goodwill and then when you have got the model, there will be an audience of people who feel, "All right, I got something out of it. I'll listen to them at least when they offer me the next step."

Kyle: Absolutely.

Andrew: OK. It is a great. It is obviously very beautifully done here. Let me bring up the site. All right, there. Why did I click on the About? I think what I should have clicked on was this big button right here, Start Saving Money, and then there is some guide on here that people can go and get for free that will sum up some of what we are talking about here and some other big ideas for them. All right, on to the next big idea on our program, which is reduce your taxes, especially in this key month. What is the key month here that I was alluding to on the board?

Kyle: The key month is December. There are a number of things that you can do throughout the year to limit your taxes and to put more money in your pocket, but especially in December. There are some important decisions that you can make that can make a very big difference to your bottom line, your personal bottom line.

Andrew: December, all right. What should I educate myself on? What should our audience educate themselves on? In fact, do you want to tell us maybe about a client of yours in the printing business as an example of what we should be doing?

Kyle: Absolutely. This is not a normal example, but we do have several clients like this. He is an ongoing client of my firm. We work with him on a monthly basis and he comes to us. He schedules an appointment with us every December to do some tax planning. We look at his numbers. We do some calculations. We looked at it, we said, "Well, it looks like you're going to owe $10,000 on your personal taxes." He asked us, "Well, what can we do?" We started asking a few questions about his business. Is there an equipment you want to buy? Are they remodeling? How old is your company car? He ended up going and contributing some money to some plans, some retirement plans, health savings account. He bought a new printer for his business and when we did his taxes for April, instead of owing $10,000, he got a $30,000 refund.

Andrew: I wasn't following. How exactly did he end up instead of owing money, getting money back?

Kyle: It sounds counter intuitive, but he was going to owe $10,000 personally, so he spent business money on equipment and by contributing to some retirement plans, these are pre-tax plans, and so by buying equipment for his business with business funds and by contributing money to retirement plans and other benefit plans, he personally benefited $40,000.

Andrew: Let me see if I understand this. He went out and he grew the expense of his business. That took his business probably from a profit to a loss, right? By taking his business to a loss, he didn't have to pay taxes and maybe he paid taxes in the past because back when he was making money, he paid taxes. Now that he is not making money, he can get a refund of the taxes he paid in the past. Is that right?

Kyle: He could have. In this case, that wasn't his situation. He didn't have the carryover losses. You're absolutely right. He took his business from a very profitable position to a loss. Because he did that, he was able to get a refund himself personally.

Andrew: Of the taxes he paid on his own salary throughout the year?

Kyle: Yes.

Andrew: OK. Got you.

Kyle: Yes. Because as an entrepreneur, as a self-employed person, you're paying the taxes. SO he was looking at his revenue coming in and paying quarterly taxes on those. At the end of the year, he essentially got almost all those taxes back.

Andrew: I see. OK. So if I'm at the end of the year and I feel like, "Whoa. You know what? Next year I'm going to have to buy computers. Next year, I'm going to have to buy other equipment. I'm going to have other expenses." You're saying take the expenses right now? Maybe next year I'm going to have to hire a team of people to go do my past interviews on Mixergy, for example and pull out the key ideas and write articles for it. I might say "You know what? Let's do it all in December. Hire all those people quickly. Pay all of them the salaries or the consulting fees that we need to. Really take the loss this year and that way I can get back some of the money that I paid earlier in the year in my tax estimates that I would pay quarterly."

Kyle: Right. Part of the equation in December is also looking at 'Where do I anticipate my business being next year?'. Are my revenues going to go up next year? Are they going to go down? Are tax rates going to change? There are a lot of different factors that come into play. That's why it's important to put a pin as to where you are now and project your revenues for the next year and make those decisions.

Andrew: I see. OK. If I were going to wait until February, for example, to redesign the site, I might as well do it in November or December and take those expenses. I mentioned earlier computers. Ordinarily, and the tax law changes, if I bought computers, hardware, equipment, like lighting or whatever it is that I need, I couldn't write it off right away. From what I understand now, I can't take my computer equipment and write off the expense immediately?

Kyle: Yes. Those hard assets like that are called capital assets. Generally you'd have to depreciate those over time. So the useful life of that asset. There's a section in the US tax code that's been enhanced since the recession started. It allows you to take those deductions, instead of amortizing it over five, seven, 10, 15 years, you can take the entire deduction at once in the current year.

Andrew: OK. Let me see if I can explain this in a more basic way and then we'll move on to the next big idea. Actually, I'll show the visuals for this idea and then go onto the next big idea. I'll keep it really simple. Suppose I have $100 worth of sales for this year. Suppose that I bought equipment for $100. In the past, the government would say "How long are you going to use that equipment?". I would say "Well, maybe four years." They would say "Great. This year you have an expense of $25. Next year an expense of $25. The year after that, $25 and the year after that, $25." So, if you have $100 in salary, you take $25 off of that as your only expense in this hypothetical example. Boom. You have $75 in profit, now pay taxes on that. That's the way I said it at first because computers are now, what was it that you said they called equipment?

Kyle: They're capital assets.

Andrew: Capital assets. Because we can all write them off on the same year now. I have $100 in sales and I bought $100 worth of capital assets, I end up with $0, nothing to pay taxes on. Did I get that right?

Kyle: Right, absolutely.

Andrew: I'm watching your face as I explain the before and after. Is there a before and after? Was it different a few years ago? I remember when I ran my past company and I bought computer equipment, my accountants told me to spread the expense over multiple years, not to take it all at once.

Kyle: Absolutely. The deduction, or the Section 179.

Andrew: Is it that it's new that we can take our capital assets and expense them all in the same year?

Kyle: It's not new. It's just that it's been enhanced. It's been broadened to capture more assets and to allow for bigger deductions.

Andrew: I see. OK. It's been enhanced now to include computers where before it wasn't?

Kyle: Computers, yes. It's been enhanced so you can include those assets. Plus, the limits were much lower before, probably, when you were doing that. Now it's up to $250,000 in one year.

Andrew: I see. OK. All right. Let's bring up this. What is a deduction? How do we know what I just discovered with you?

Kyle: This is a really simple equation. It goes back to the beginning. How do I reduce my taxable income? There are a number of different ways of doing that. The easiest way is by tracking those business expenses that you're already incurring in your business. It's a plus-minus game. The plus is the revenues. The minus is your business expenses. That gives you your taxable income. Those deductions are just those expenses that the government recognizes as valid business expenses that reduce that taxable income that you pay taxes on.

Andrew: I've got another visual here but I think we've got this idea. Should I show this other visual? Is there more you want to say about it or should I move on to the next big idea?

Kyle: I think we've covered that one pretty well.

Andrew: All right. Next one is "Know the right time to track your expenses and how". What do you mean by that?

Kyle: It's interesting. I run into a lot of startups, a lot of entrepreneurs who start investigating businesses, they start spending money by doing research, by going to conferences, by talking to people, by even testing in advertising, even buying Google ad words. That type of stuff. Then they don't keep track of those expenses and then when they get into business, they have no record or they haven't deducted those expenses. Those are all called startup expenses. I don't mean to be demeaning. It sounds stupid. Of course those are startup expenses. But most people don't track those expenses as they're incurring them. The tax law says that if you don't deduct those expenses the first year you're in business then you've lost the ability to deduct those.

Andrew: What you're saying is that most people in their first year of expenses say, "You know what? I've got all these expenses. I'm buying Google ads as you said. I'm trying to buy an ad on Facebook. Someone told me about some Twitter something. I'm going to buy that." I'm not going to keep track of it because I'm running a business and, frankly, I don't have anything to expense it against. I have no profit. So if I have no profit I'm going to pay no taxes anyway. I have no sales. So who cares about the expenses? I have no sales, I don't care about the expenses because I'm not going to have a profit and they only tax profits. You're saying, look, the government is telling you that you better keep track of these expenses right now and in the future, if you have a loss this year, in the future, it's going to be counted against your profit. Do I understand that right?

Kyle: Right, yes.

Andrew: I see. OK. That's why. Even if you don't have a profit now, think ahead, entrepreneur. You, at some point, are going to have profits and you're going to now be able to shield some of those profits by taking count of your expenses now.

Kyle: Absolutely. And a lot of entrepreneurs I run into don't do that. They think "I don't have a business yet".'.

Andrew: Your first example, right, did you have this issue when you were starting out?

Kyle: I did.

Andrew: Do you want to open up and tell us about that?

Kyle: Absolutely. I started doing a bunch of research. I took courses. I flew around to conferences. In fact, I went to a conference where the total fees, the conference fee and lodging fee, was about $3,000. My wife came to me, this is before I went and got my post doctorate in tax, she said "Listen. The limit for these expenses", at that point, '"as five thousand dollars. You're bumping against those $5,000. We have to start the business now or we're going to lose the benefit of some of these expenses". Now, the limit is $10,000. So if you're getting close to the $10,000 limit or if you're incurring all those expenses and you're getting close to $10,000, it makes sense to make the decision to start the business and take the couple of steps to make this venture look like a business.

Andrew: What's the $10,000 number? I know at the time you were doing this it was $5,000, now it's $10,000. $10,000 for what? I can keep no more than $10,000 of expenses for the future?

Kyle: No. The startup expenses, you're limited to deducting $10,000 in startup expenses in the first year. Let's say, you go out and do a bunch of research. You set up the company, you have $10,000 worth of expenses. You can deduct those in that year.

Andrew: I see.

Kyle: And you have to deduct those that first year or else you lose them.

Andrew: But I can't deduct any more than $10,000 is what you're saying.

Kyle: Well, this is where people run into trouble as well. There's another tip. This is why I say to start the business before you get to that $10,000 limit. Let's say you spend $20,000 before you start the business. You can take the $10,000 but that extra ten grand, you're going to have to depreciate or you're going to have to take those expenses over 15 years. The benefit is miniscule.

Andrew: I see. OK. All right. So if I'm spending $100,000 in startup expenses because I'm deciding that I'm going to really invest in my business and getting ready for the business and exploring ideas. $10,000 I can't write off the future. I can expense it this year but I can't get the benefit of that next year. I have to take it over several years.

Kyle: Right and, in fact, if you go over $60,000, then you loose the benefit all together at some point so, it's a sliding scale and it starts to get convoluted. That's why I recommend to people, if you get close to that $10,000, start the business. And then, you don't have to worry about all, it makes it simple..

Andrew: What's the difference between starting the business and not starting the business? Is there an official act that you go through that starts the business?

Kyle: There really isn't so, what the IRS looks at is, they look at your intent at that point. So they look at have you filed for a business license? Do you have an EIN? Have you incorporated? Have you actually offered goods to the public? That's one of the criteria the IRS looks at to.

You don't even have to go and incorporate and do all the other stuff. You just have to actually start selling something to the public.

Andrew: I see. You need to do something that shows that you have an intent to really have a business here and we'll talk more about the difference between a business and a hobby and how the government looks at it, not how you look at it.

You just need to do something that shows "Hey, this is a real business. I'm not just going to seminars because I enjoy hanging out with people and learning." Got it.

EIN is what?

Kyle: It's an Employer Identification Number. It's basically the Social Security number for your business.

Andrew: Every entrepreneur who's gotten one knows how many times you have to repeat it.

Let's bring up this quick visual, by the way, largely because I just love the design on your site. This is off your site. What is this and how does it factor into this idea that we're covering right now?

Kyle: I show in this diagram, you got the idea on the left, you got a bunch of expenses before the business begins and a bunch of expenses after. The expenses are the same. Start up and operating expenses are the same type of expenses except the start up expenses are limited to that $10,000 in the first year of operations.

Andrew: OK. If you can't see it because you're listening to the MP3 or reading the transcript or if I don't have the right resolution here in the video for you, don't worry, it will be included with the program notes here so you'll have a clear vision of it. And I say that, of course, to the people in the audience.

Anything else before we move on to the next big idea?

Kyle: No. I think we've covered it.

Andrew: I think we're going at a nice pace.

All right. Next one is Avoid the equity is free pain.

Kyle: Yeah. This is another one of these eye-opening issues that I hate to see people run into inadvertently and I tell people remember equity is not free and that means, if you are receiving equity from a business, if you haven't contributed some tangible property to that business, then you're going to be taxed on the value of that equity.

Andrew: Can you illustrate this with an example? I want to make sure that we understand this.

Kyle: I can. I had a client. They're a company in California. They're a software development company. They're boot-strapping the company, as many of them do and they just gone through a round of funding. They received a valuation of about $1 million and they still didn't have the funds to bring on as many developers as they needed so they offered some people equity in the company.

Andrew: Standard practice. You don't have enough money to pay your employees or you want to really get them excited, you give them equity.

Kyle: Right. Exactly.

Andrew: I'll give you a share of the business, you'll have the upside. You believe enough in me to work here, you don't want just the salary. That's why you're working at this startup. I'll give you equity, a piece of the pie. OK.

Kyle: Right. So each of these developers received 2% and there was 3 developers. They each received 2% of the pie, of this million dollar pie.

And they came to me and said 'Hey, we did this. We need to work out a few other things.' I looked at it and "Well, did you tell these guys that they're going to be taxed on $20,000?" and it was dead silence in the room and they're like 'Oh, shit. How do we explain this? We hosed these guys.'

Andrew: Right. So you are saying you give them 2% of the business, not cash, 2% of the business. That's worth $20,000. The government says, "You just got $20,000 in value, you better pay taxes on this" so now these developers who didn't get cash, have to go around and find cash to pay taxes because the Government is not going to take a percentage of the business. They need the cash equivalent of their share.

Kyle: Right.

Andrew: I see. So then, at that point, you have to really start hitting people up for cash. We've seen this happen in the past. That's because equity isn't free to the recipient. You still have to pay taxes when you're being given equity. What should we do instead with our employees who we value, we want to make sure they're not hit with the tax bill for an asset that's really not worth that much and not sellable until some point in the future?

Kyle: I recommend options. Options to acquire equity is the best route to go. If the business does become something, they're not taxed when they get that option unless they choose to be taxed. They won't be taxed on it until they exercise the option.

Andrew: Options, not stock. Just recognize that if you ever give someone stock and there's a value on the company they're going to have to pay taxes on their share of the value they're getting.

Kyle: Absolutely.

Andrew: What is this?

Kyle: This is a diagram to show what we call the equity tax bite. You've got a million-dollar business. If a service provider comes along and provides a service, it's a service, not contributing property to the business, and they get 5%, then that service provider is going to be taxed on $50,000 worth of value. That's not capital. That's $50,000 of income. That's an income tax rate. It's not the capital tax rates, which are lower right now.

Andrew: By the way, how are you feeling about this? I know you had a lot more visuals you wanted to show. How are you feeling about the way we're explaining these topics with a few visuals and a lot of stories?

Kyle: This is great. This is fantastic. Generally, people hear tax stuff and they say "Oh, my God. I'm just going to tune out.". Their eyes glaze over. Generally, it's not nice to know stuff. You need to know stuff. That's the goal. I'm glad you're doing this, showing this stuff in an interesting way.

Andrew: Good. I appreciate that you're saying that. I know how important it was to you that you get this explained properly and so I thought I would check in with you in public to say "Am I doing a good job here? Am I helping you communicate these ideas right or am I doing justice to these ideas?" I'm glad you're saying yes. So onto the next. The next one is to create the schedule you need. I alluded to the schedule that you have in our notes. But you tell me. You tell the audience. What's the schedule you need to put together? A schedule of what?

Kyle: It's a schedule of when you need to file tax returns and to pay taxes. As an entrepreneur, you're inundated with deadlines. Deadlines from vendors, from customers, from whomever. But you have a ton of deadlines to meet from the government as well. The best way I recommend to deal with those is to set up what's called a tax calendar at the beginning of the year. Look at "What do I have to file this year? What do I have to pay?" and just go in and put those into your Google calendar or whatever and set alerts for them and it's off your mind.

Andrew: Do you have a client that you did this with that maybe we can use as an example?

Kyle: I did. She came to me, as many of my clients did, because there was a raging fire already because she didn't set these alerts. So she was relying upon her accountant at the time. I always tell my clients to make sure to do this stuff yourself because in the end it's your a*s on the line. It's not your accountant's, it's not your tax attorney's butt on the line. It's yours. It behooves you to do this stuff yourself.

Unfortunately, she had relied solely upon her accountant to remind her and to do these things. That accountant had had some health problems, she had had a death in the family, she fell off the grid and didn't take care of a couple of these things and as the government generally does, they're slow to catch these things, but interests and penalties are building up. So she came to me. She had missed a filing deadline and it was three years later. Her bill was $46,000 because of the interest and penalties that had accrued on this somewhat small amount that she should have paid three years ago.

Andrew: This is giving me a pain in my stomach but I will find a solution for this. I didn't know that I needed to keep track of my own stuff. I know that I've missed some because my accountant was the accountant that I had back in the Bradford and Reed days. Back when we were pulling in millions of dollars and I was an important account to him at that point. Now, everything is on auto pilot for him for revenue, right? I am not a huge client for him. He knows basically what he could expect from me. He is not alerting me and frankly, when I was traveling all over the world, when I was living in Argentina, I wasn't touching in with the account the way that I was before, so shame on me there, and now it is time for me to keep track of all the deadlines myself if only to make sure that he is telling me about them.

I accept what you are telling me and I know when you say use Google Docs, Google Calendar, fairly easy to do. Frankly, I use Google Calendar for national holidays. I don't book an interview on a date that I know that the Kyle won't show up because he has a picnic and forgot about it. I now have it. I know how to do that. I don't know where to find these deadlines to put on the calendar. How do I do that?

Kyle: Well, it does make it somewhat complicated because you are going to have federal, state, local, a bunch of filing obligations. For all the federal obligations, you can get to the IRS website. There is a link. You can download and you can actually order a paper calendar if you want.

Andrew: How about now?

Kyle: You can download a copy of the federal. . .

Andrew: Paper calendar?

Kyle: Yeah. You can get a paper calendar.

Andrew: You know, I am looking actually over your shoulder and I see all the different machines that produce paper. It makes me uncomfortable. You are in a very paper-based business.

Kyle: I am, but I have to tell you in the last year, my firm. . . I like to go minimal paper. We have used less than two reams of paper in the entire year.

Andrew: Oh, good. That is impressive.

Kyle: I don't like paper. I don't like the paper calendars, but some people do.

Andrew: Okay. You are saying I can ask them for a paper calendar or is this the URL right here? The one that we can go to? Let me zoom in at the bottom here.

Kyle: Yes.

Andrew: Zoom and move up. It is this URL right at the bottom?

Kyle: It is, yes.

Andrew: That is where we can go and we can get the federal tax calendar.

Kyle: Absolutely.

Andrew: Okay.

Kyle: You are right. Right now, there are a lot of. . . And you can see towards the top, there are a lot of filing and paying obligations and unfortunately, it is incumbent upon you to go out and to talk, get on the websites of your state and local entities and figure out when you need to do this stuff. Most of it is generally, for smaller businesses, on quarterly basis. Because this is such a pain point, one of the things that Nick, my partner, tax receipts and I are doing is we are working on a tool that will help automate this process for entrepreneurs and remind them.

Andrew: Bless you, yes. All right, but for now, this is a URL of course we will include if you guys are listening and you don't see it. The URL is up there on the screen. We will have it in the course notes and of course, we will have the screenshot in there, too. In this screen shot, you are going to have an understanding of the kinds of things you should be prepared to file and to pay and what I am taking away from this is that I should just talk to my accountant and say, "Look, I got my Google Calendar here in front of me. Tell me what's coming up for me or better yet, email it to me. That way, I have a good record of what you told me and I don't miss anything."

Kyle: Absolutely.

Andrew: OK. All right. Let's see. That is the way to create a schedule. Let us go on to the next big idea on the big board, which is not taxes, getting your travel, there we go, in real time. Getting your travel subsidized. That means that, well, you tell me. What does that mean? How I can get the travel that I take subsidized?

Kyle: Well, Uncle Sam will subsidize your travel.

Andrew: Did you do this?

Kyle: I am a big fan of traveling, yes.

Andrew: OK. How did you do it? I don't want to put you on the spot here, but I see here on the notes that there is a hint here that you did it and so I figured I will talk to you about that.

Kyle: Yeah, yeah. I like traveling so I generally turn it into business travel because then it becomes subsidized by the government.

Andrew: OK.

Kyle: I was going to Europe last year for some business and instead of hopping on a flight, I hopped on a cruise ship instead and the mode of transportation was irrelevant in that case and in fact, you get a much bigger allowance, or this is an allowance. There is a limit for the amount you can deduct when you take a cruise ship, but it is ridiculous. It highlights that you can subsidize some of your travel by integrating it in your business.

Andrew: OK. If I take a cruise ship to get to Europe, the cruise ship expense even though I am having a fun time on the cruise ship, that is an expense that I can write off. How else can I do it if I can't take a cruise ship to a meeting?

Kyle: Well, if you are, let us say, in the United States, if you're going for travel, and if more than 50% of the time you're spending on that travel is for business, then you can deduct all the cost of that transportation plus any of the business related expenses. So, any of the lodging, any of the actual meals, the business meals you can deduct. That's just if you're spending more than 50% of your time on the business.

Andrew: OK.

Kyle: Once you get outside the United States, the rules can be much more complicated. One way to simplify it is to take a trip that's less than 7 days that's outside the United States, and it's the same rule.

Andrew: OK, and of course we're going to have this up for people to see this flowchart. Is this flowchart complete, is there anything on that's not on here that we should be aware of?

Kyle: No. Most of it is covered, I would just say if you have any questions about this, or if your situation doesn't fit within this, then talk with your tax adviser. If your trip goes over 7 days and you're overseas, as long as you spend more than 75% of your time on business, then the rule is the same. You can deduct all of your transportation.

Andrew: OK.

Kyle: So, either make your trip less than 7 days or spend more than 75% of your time on business so you can deduct all your transportation.

Andrew: Alright, so if I have a trip that's a legitimate business trip that takes 10 days, I can invite my wife out for 9 of those days and we can have a good time in the city?

Kyle: Potentially. It depends on, of course, because I'm an attorney, I have to say it depends.

Andrew: It depends on what? I know that this isn't going to give us a thorough understanding, but give me a general understanding of what I'm missing there because I thought I was doing the standard math easily. If more than 50% is on business, you can take all those deductions.

Kyle: Oh, you can yourself.

Andrew: Yeah, that's what I mean. Oh, I see, because I said the wife, now suddenly that's different. OK.

Kyle: Now, let's say, let's say you hire your wife.

Andrew: I see.

Kyle: There actually are some opportunities there for planning. So if you hire your wife to do some business, and she comes out and does some business for you. You have to be careful because you have to document it properly because you're what's called "related parties", but you may be able to deduct your wife's transportation as well.

Andrew: I see, so I'm going to a conference. My wife is going to man the booth when I'm on stage, I'm going to man the booth when she's on stage, we're both working the conference for ten days. We're done with the conference the other nine days, we can take another nine days and just have a good time in the city.

Kyle: Yes, absolutely.

Andrew: And all that's documented, OK. What about weekends, by the way? What if I'm only Friday on a conference, because I've seen that there are some organizers that do their conferences on Thursday or Friday, let's say I'm doing it just for Friday.

Kyle: Right.

Andrew: I want to stay for Saturday and Sunday for the weekend. Those don't court, right?

Kyle: Well, they're not business days, no. What a lot of people do, especially outside the United States, is they'll sandwich conferences or meetings. So, if your conference ends on Friday you schedule a Monday meeting, or a Monday lunch with somebody or something like that. And then the entire weekend is considered in that realm and you're covered then.

Andrew: We talked a little bit about hiring my wife. If I hired my wife, it wouldn't be as a full time employee. In fact we don't have any full time employees here. We have contractors, which brings up the topic that I didn't put up on the big board, but started to do because I want to talk about it. It's how to treat employees versus contractors. What's the difference? We only have contractors here at [??] employees. What's the difference and, how do we do this right?

Kyle: So, the IRS, and a lot of different federal and state agencies are really sensitive to this employee-independent contractor debate, so it's important to get this right. Independent contractors essentially are self-employed people, they have the risks of taking on the job, they have to pay their own taxes, and an independent contractor also has the right to set his or her own hours and essentially just deliver a product to you as the hiring firm.

Andrew: I see, so, before we even go to that, I wanted to make sure people understand why this is important. I want to make sure I'm understanding why it's important. The reason I don't have employees is I don't want to have to pay taxes for them. I don't want to worry about hiring and firing them on a certain date. I don't want to have to worry about the local laws here. There are other issues. I might want to travel to another country and I don't want to have someone in the office. But those are the benefits I imagine. I'm learning throughout this session that I was wrong about a lot of things. Maybe you can tell me. What are the benefits of contractors over employees that make entrepreneurs want contractors and not employees?

Kyle: The biggest one is that employees are freaking expensive.

Andrew: Expensive how?

Kyle: Expensive in that you have a lot more administrative overhead. You have a lot more filing requirements if you have employees.

Andrew: Filing requirements? Do I have to pay taxes on their behalf?

Kyle: You have to pay taxes not only on their behalf but for them. So if you're a W2 employee, you have a withholding from your paycheck. Your employer generally has to match that withholding. That's only one half the equation. The employer is paying the other half of the payroll taxes. Then there's unemployment insurance, worker's compensation. There are all kinds of employment laws and discrimination things you have to worry about and concern yourself about with employees. If you can help it, if you're a small business and someone's doing something that isn't necessarily integral to your day-to-day operations, then I do recommend that you use independent contractors.

Andrew: OK. All right. The reason we're having this conversation is we now see all the benefits of having contractors over employees. But if we have contractors who are essentially employees, the government says "Hey, wait. You're trying to get away with something. All those things you thought you didn't have to do? Now you have to do them retroactively." So what do we do to make sure that we keep contractors as contractors and not accidentally trigger this employee thing?

Kyle: I gave you a graphic.

Andrew: All right. Let's bring that up. I'd love to get an example also so that we can include that. But first let's get into what we need to do. Here is the graphic.

Kyle: There's a lot of text on here. Essentially, this is a checklist to look at; some criteria of what's an employee and what's an independent contractor. What does one look like and what is the other? A lot of it comes down to the independent contractor works for him- or herself whereas the employee works for you. It's important to keep these criteria in mind when you're setting the hours, the requirements on the independent contractor. The way you do that, the first step is to have a contract with that individual independent contractor that lays out what's required of the contractor.

One of the things that did happen., I had a client who's a software vendor. They had an independent contractor that was doing all of their inside sales. That's a fairly integral part of their business. The company told the contractor when to come in, where to work, how to work and said "But, you're an independent contractor. You're on your own for your taxes." This client was audited by the state of Washington and the state of Washington looked at it and said "This person is not an independent contractor. Regardless of what you say he is, he meets all these different criteria for an employee. So guess what? You owe us all the back unemployment taxes, all the back payroll taxes, interest, penalties, workers compensation". And then, to add insult to injury, the IRS came along and audited them as well and slapped them with the same thing. So they ended up with a $40,000 bill for one year for not treating this independent contractor like an employee.

Andrew: $40,000 for one year for one employee? Wow. All because they weren't aware of this chart that we're going to be giving people. This is yours. It looks beautiful. Is this something you guys put together yourselves? It's based on a set of guidelines that are publicly available, right?

Kyle: It is, yes. It's something we did put together but it's just some guidelines. These are general criteria that a lot of these government agencies use to look at whether someone is an employee or an independent contractor.

Andrew: OK. All right. You can't pretend that they are a contractor and then make them work at a specific location, come in at a specific time or else they are in trouble with you, work a specific amount of time, etc. This will all be in the course notes, thanks to Andrea who is a contractor here and she is so good that she actually gave me the contract as she was the first contractor that I hired.

Kyle: Good on her.

Andrew: Yeah, right on. Thank you, Andrea. She is used to doing work like that so she set us up. All right, so next big idea is establish your tax home. I am a globetrotter. What does this mean?

Kyle: I can start off with a story about that.

Andrew: Yeah, please.

Kyle: I had a software developer client and he loved to travel as you do, as I do, and he would be hired by firms all over the world and he instead of establishing a business, a tax home here in the United States, he could just go and get a new mailing address or didn't have a mailing address and would move around every three months or so as he got these projects. He came in and he wanted to get his taxes done with my firm and we had to give him the bad news that because he had been moving around and never established himself in what is called a tax home, a regular place of business, that he would be classified by the IRS as a transient and couldn't deduct thousands of dollars he had spent moving around the world.

Andrew: A transient? That is an official classification?

Kyle: Yeah. It is pretty harsh. It is pretty harsh, but there are just a few simple things you can do.

Andrew: Yeah. What do I do now to avoid being a transient? First of all, I like the title of transient, but if it is attached to all these penalties, I don't want to be a part of it. What do I do to keep from making that mistake?

Kyle: Well, the first thing to do is establish. . . To establish a tax home, you establish a regular mailing address, a regular place of business. Even if it is like your parents' house or a friend's house, some place where you receive mail on a regular basis and is determined by your state to be your place of business. If you go and get a business license in your state and say this place, this mailbox, this UPS store or my parents' house or whatever is my place of business, then you have established your tax home at that point.

Andrew: Ah, I see. OK. I have done that, but I didn't realize that that is what we were doing. I have had the same mailbox in California for years even as I travel and have been paying tax in California and you are saying a mailbox is legitimate.

Kyle: Yes, yes.

Andrew: If that is where I get my paperwork, that is where I get paid by my customers and so on. You just need at least one place that you make your real home even if you are not really living in it.

Kyle: Right, right. It is important also, let us say, where you do your business on a regular basis, let us say you are a consultant and you work out of your home for instance, if you don't establish that as your place of business, then anytime you go out to somebody's office to do a job or you fly somewhere to do a job, those expenses are not going to be deductible because you haven't established that tax home.

Andrew: I see.

Kyle: Then moving around out of the country, there are some other things you can do. They get kind of complicated, but if you are moving around a lot and outside of the country, then stay out of the country for over 330 days. As long as you are outside the US, you can potentially take advantage of another tax deduction that allows you to exclude all of that income you receive while you were overseas or, I am sorry, up to about $93,000. It is $92,900.

Andrew: I could have excluded that much money out of my income when I was living in Buenos Aires.

Kyle: Yes. Yes. If you are out of the country for 330 days or more, you have an exclusion of almost $93,000 and so that means you don't pay tax on that $93,000.

Andrew: This is the worst course I have ever done. It is just me getting kicked in the teeth. I wonder if we did that. I need an accountant who can really have a conversation with me. Are you available? Can I hire you? Can other people hire you?

Kyle: Absolutely. Bring it on.

Andrew: Where do you live in Seattle?

Kyle: No, no. I have an office here in Seattle. We also have an office in California.

Andrew: You do? What if I don't live in California anymore because I'm a, what's the word you used?

Kyle: Oh, you're a transient. That's right.

Andrew: Transient. Then maybe we can't work together, right? You're more California and Seattle?

Kyle: Yes.

Andrew: All right. OK. Because, you know what? I was scrolling through your site earlier and I said "Where's the contact information? ". Where is the contact information on here?

Kyle: Yes. It's still in its initial beta stages here, so this is good information for me to learn, too.

Andrew: Yeah, contact information is really good. I could use it. Usually, I don't care. I don't want to contact anyone, but this is great. This is, by the way, what people can get from you. The over 1,000 pages of tax regulations on a business card. This is where you give people some guidelines that they should keep with them.

Kyle: Yes. We have a couple things on the site. That's one of them. You can download the card. We have hard copies we'll send as well. It's just while you're traveling around, it reminds you of things to keep track of.

Andrew: There's the plain English deduction guide, what else is there? All right. You're really at the point with the site where you're in the giving, giving, giving mode. I don't even see a place where I can give you my credit card, where I can give you my email address. Who knows?

Kyle: Yes. As you mentioned, we're in the start-up phase. To be completely transparent, we have established some partnerships with some companies. Quickbooks is one of them. Shoebox is another one.

Andrew: Yeah. I saw that. Basically what it means is you're linking over to them. You're at the place where my audience should really be jumping into this site because this is the place where you guys are eager to give. You guys are eager to figure out what problems people have when it comes to taxes. This is the stage where it's really good to be a part of it. Especially if the guy behind it knows his stuff, which you do. I've got one visual for this section, which is "Establish You Tax Home". Why don't you quickly give us an understanding of what this visual is that we're looking at and then we'll move on to the next one. Of course, we'll hand this out and everyone will have it with them.

Kyle: Let's say you run a home office. Anytime you go from your home office to a temporary work location, those expenses are deductible. Those transportation expenses are deductible.

Andrew: If it's from a home office to another, like, to a coffee shop where I'm going to be working or one of these day offices that I sometimes have rented in the past, that trip is deductible?

Kyle: Right. Exactly. Exactly. Let's say you have an office also. Anytime you're going from your home to your office that you pay for, that's not deductible. That's a commuting expense. Commuting expenses are not deductible. But, if you went from that external office to a work location to meet someone, to work at their place or to meet somebody at a coffee shop, that's deductible. The only time it's not deductible in that transportation scenario is if you're going from your home to your office or vice versa.

Andrew: Commutes you can't expense, you're telling me? I can't deduct them but transportation while I'm at work or after I've gotten to my desk is deductible?

Kyle: Yes.

Andrew: Let's look at the final big idea. The final big idea is act like a business or else. Before we get to the 'or else', what's the alternative to acting like a business? A hobby?

Kyle: Yes. Absolutely. That's exactly what it is. That is the word you never want to hear come out of an IRS auditor's mouth is hobby. Hobby means that you can't take losses. Those are losses that exceed the amount of revenue you bring in. If they call your business a hobby, you can take losses up to the amount of revenue. Let's say you take in $10,000 that year, you can take losses up to $10,000. A lot of people, though, when you're in this startup phase, you have losses that exceed your revenue. Obviously. You want to be able to continue rolling those losses forward to offset income in the future.

Andrew: That's the key. If you have a lot of losses in the first couple years of your business and in the next few years, you're suddenly bringing in money, you can counteract the profits with the losses from the past. As bad as you feel about losing money the first few years of running your business, at least there's an upside, which is in the future, when you do make money, you can write off some of that profit. You can take deductions against some of that profit.

And so, unless it's a hobby, unless they say 'Hey, you know what, Andrew? I'm excited that you are doing this video show on the internet but, really, you got all these expenses in bandwidth, all these expenses in computers, best buy some shaky expenses that we can't prove but let's suppose even then that's terrific. There's no revenue here. It's not really a business. It's just really you entertaining yourself with your new Apple computer, it's a hobby. I don't care how much you lose, you can't write it off against other profits that you have.', that's the danger. That they think that this is a hobby.

So how do I keep them from thinking that my business is a hobby, whether it's this or software creation?

Kyle: It's to treat it like a real business. So, if you, let's say you set up a separate entity for it, you go start an LLC for it, or you're starting a corporation for it, you're fairly protected then. There have been cases where people have gone and set up LLCs and they've been in trouble because they haven't really treated it like a real business so, instead of, they go to set up the LLC but they're still using their own bank account to fund it. So, if you set up separate books, separate LLC or separate entity for this and then treat it as a real business showing that you're actually trying to make a profit with this business and that's the key the IRS looks at, is there a profit motive with this business?

One of the questions on our site, you look at our site and, like, I don't see the profit motive. Well, that's because we're still on this testing phase and giving people information, seeing what people need and that's what a lot of businesses are, the testing and trying. The IRS looks at did you try to make a profit in 3 out of the last 5 years? If you have, then you fall within what's called the Safe Harbor. And so, if you attempted to sell something, attempted to make a profit within 3 out of the last 5 years, then you're protected to a great extent from being called a hobby.

Andrew: I see. So the very least, I should be trying to bring in advertisers with whatever I'm doing or at the very least trying to sell back interviews or something, or else they're going to say 'You can't write off all the expenses associated with it.'

Kyle: Right.

Andrew: You had a, did you work with a documentary filmmaker? Can you tell us that story?

Kyle: I didn't but this is a case out of Arizona. And this filmmaker, she had a legitimate business. She set up an LLC. She was an attorney so this was a side deal for her and she went out. She created this documentary and it won a couple of awards, some film festivals. It was shown all over the country. The IRS audited her in 2010 and said "This is a hobby. You have all these losses. You have a full time job, this isn't a real, you have no profit motive here either because this is a documentary. It's educational."

And so, they went and slammed with $300,000 worth of back taxes on this hobby, even though she did have a business entity set up for it. She made a few critical errors that they cited and she's still appealing. It'll be in the courts for years.

Andrew: And I can see that. Frankly, it does take a while for tech entrepreneurs just to bring in revenue. It takes a while for mobile apps and for the industries frankly that we're targeting. It takes a while for the whole industry to start producing revenue, let alone one company. You are saying, do some of the things that prove that you're a real company. Take it seriously. Don't use the same bank account for your company as you do for yourself. Don't forget to think about revenues and to maybe start putting some plans in place to bring them in.

That makes a lot of sense.

Kyle: And there's one thing, if I could add one thing here. There is this one, again it's almost a myth, and I don't want to give people impression of this myth. If you don't make a profit in 3 of the last 5 years, that doesn't mean you're automatically a hobby.

Some people have come into my office, some entrepreneurs and they're like, crap. We have to start making money immediately or I'm going to be hosed. And that's not the case. That's just one of those criteria the IRS uses. It's a Safe Harbor. So, if you do make a profit in 3 of the last 5 years, you're safe but if you don't that doesn't mean you're screwed. You just need to treat it as a real business.

Andrew: All right. So guys, as you saw, we put a lot of work into this. We have a lot of notes, we spent a lot of time picking out just the right ideas for you and making sure they're explained through examples and through charts. But of course, all we are doing here is giving you an understanding that, well, we're not replacing your accountant, I want to say over and over.

I want to say that because it's at the top of the notes and it seems like it was important to you, Kyle, that we mention it twice. We're not replacing your tax or legal advice. What we're doing instead is saying "Here's a better understanding that you might have gotten. Here's some things that you might want to go over to your accountant and talk to" and, in my case, it was, where is that one slide? This is one that I'm going to have to go and talk to my accountant and say "Hey, help me put this together." In other cases, it'll gave me an understanding that I couldn't have done on my own.

Regardless it's there for you to help you improve your business. If there is one thing on this big board that you can use, use it and then come back and let me know how you've used it.

And, as I mentioned throughout, this is Kyle's site, go to taxreceipts.com. You got a great domain. You guys are feeling comfortable with saying how much you spent to get taxreceipts.com as a domain.

Kyle: You know, my partner, he acquired it for a pretty good deal. It was pretty good.

Andrew: All right. I know the way you guys operate. He's handling the tech side of things and eventually the revenue when that comes in and he picked you for the same reason that I picked to have you here. Because you know your stuff when it comes to taxes and you know the issues that entrepreneurs like me face.

So, I appreciate you doing this session with us. Thank you for teaching us, Kyle and the website is taxreceipts.com and thank you all for being a part of this program. Looking forward to hearing your feedback. Bye.

Kyle: Thanks for having me.