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Accounting & Legal Issues For eBay Sellers

This information as shown here, was presented in its entirety in meetings and workshops held at the *eBay Live 2004* Convention in New Orleans, LA

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Accounting and Legal Issues for eBay Sellers

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I. Introduction

- A. Importance of taking advantage of tax write-offs: To keep more of the money you earn.
 - 1. Report your income and claim allowable deductions and credits.
 - 2. Work with a tax advisor (80% of small business owners use an accountant).
 - 3. Use bookkeeping software (e.g., QuickBooks) to simplify recordkeeping for tax purposes.
- B. Importance of adequate insurance coverage: To protect yourself from financial devastation in case of disaster.
 - 1. Work with an insurance agent.

II. Home office deduction

- A. Qualifications
 - 1. Use space in your home as the principal place of your eBay activities.
 - 2. Use the space regularly and exclusively for business.
- B. Scope of the deduction
 - 1. Home office deduction = all "direct expenses" plus portion of "indirect expenses."
 - 2. "Direct expenses" are fully deductible as part of the home office deduction (no allocation required)
 - a) Examples: Painting a home office; electrical work to the office.
 - 3. Figure percentage of home office use on a square footage basis

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- a) Example: If your home is 2,000 sq. ft. and you use 200 sq. ft. as a home office, then 10% of indirect expenses are part of the home office deduction.
- 4. Figure portion of home office use on the basis of the number of rooms if they are of approximately equal size.
 - a) Example: If you have six rooms, all of approximately the same size, and you use one as a home office, then 1/6th of indirect expenses are part the home office deduction.
- 5. Examples of "indirect expenses":
 - a) Rent if you lease; depreciation if you own
 - b) Real estate taxes if you own
 - c) Utilities
 - d) Maintenance
 - e) Alarm system monitoring fees
 - f) Insurance
- C. Resources:
 - 1. IRS form for claiming the home office: Form 8829.
 - 2. IRS publication on figuring the deduction: Publication 587, Business Use of Your Home.

III. Insuring your home office

- A. Check the scope of your existing homeowner's policy
 - 1. According to a national survey by the Independent Insurance Agents and Brokers of America, Inc., almost 60% of home-based business owners do not have coverage.
 - 2. Check for liability coverage
 - 3. Check for property coverage
- B. Consider amending your homeowner's policy to upgrade to your needs (for example, include adequate coverage for your computer and other business equipment).
 - 1. Cost: As little as \$25
- C. Consider buying a separate policy to provide adequate coverage.
 - 1. Cost: As little as a few hundred dollars

2. Probably need separate policy if storing inventory at home.
- D. Create a disaster recovery plan
1. Back up computer files.
 2. Keep back up offsite (e.g., back up to Internet site or store tape backup in a safe deposit box).
- E. Resources:
1. Insurance Information Institute at www.iii.org/individuals/business/buyingandsaving/homebusiness.

IV. Furniture and equipment

- A. First-year expensing
1. Deduct the cost of equipment in one year instead of writing it off over a set period fixed by law (generally five or seven years).
 2. "Equipment" includes items such as a computer, cell phone and desk.
 - a) Off-the-shelf software also qualifies for expensing.
 3. Dollar limit on expensing in 2004 is \$102,000.
 4. Property must be placed in service by December 31, 2004.
 - a) Property purchased for personal use before 2004 and converted to business use in 2004 does not qualify (although it may be depreciated).
 5. Property can be new or used.
 6. Property can be financed.
- B. Bonus depreciation
1. Deduct 50% of the cost of equipment (minus any first-year expensing) in the first year.
 - a) Note: Bonus depreciation set to expire at the end of 2004 unless Congress extends it.
 2. Only applies to new (not used) property.
 3. Election to waive 50% bonus depreciation in favor of 30% bonus depreciation or no business depreciation.
- C. Generally, expensing is preferable to depreciating property
1. Immediate and full write-off.

2. Simplified recordkeeping.
3. But expensing is allowed only to the extent of taxable income from a business (if unprofitable, there is no immediate benefit to expensing).

D. Resources

1. IRS form for claiming first-year expensing and depreciation: Form 4562.
2. IRS publication on depreciation: Publication 946, How to Depreciate Property.

V. Travel and entertainment expenses

A. Use of your car

1. Deduct either actual operating costs or use the IRS standard mileage rate (37.5¢ per mile in 2004).
 - a) Applied to car that is owned or leased.
2. Keep detailed records of car use (date, starting and ending odometer reading, destination and purpose of the trip).
 - a) Use a diary, logbook or electronic recordkeeper.

B. Meals and entertainment

1. Deduct 50% of the cost of entertaining vendors and other business associates.
 - a) Cannot deduct your own in-town meal costs, even if business-related.
 - b) Can deduct your own meal costs out-of-town (e.g., at this convention).
2. Keep detailed records of meal and entertainment expenses (date, cost, person being wined or dined, purpose of the expense).

C. Conventions and seminars

1. Deduct full cost of lodging and transportation costs, plus 50% of meal costs.
2. Deduct registration fees.

D. Spousal expenses for travel and entertainment generally not deductible.

1. Exception: If spouse is your employee and expense is business-related.

E. Resources

1. IRS publication: Publication 463, Travel, Entertainment, Gift, and Car Expenses.

VI. Retirement plans

A. Shelter your earnings and save for retirement by contributing to a qualified retirement plan.

1. Can set up a plan for a part-time or full-time business (even if you are covered by an employer's plan for your day job).
2. Have until the extended due date of the return to fund the plan.

B. Plan choices

1. Profit-sharing plan.
2. SEP plan.
3. SIMPLE plan.
4. 401(k) plan (even for one person).

C. Credit for setting up the plan

1. Credit is up to \$500 per year for three years.
2. Only applies if the plan covers at least one person who is not the owner or owner's spouse.

D. Resources

1. IRS publication: Publication 560, Retirement Plans for Small Business.

VII. Other deductions

A. Supplies (e.g., packing and shipping materials).

B. Legal and accounting fees.

1. Fees related to setting up the business can be amortized (deducted ratably) over a period of not less than 60 months.

C. Banking fees

1. Monthly account fees.
2. Merchant authorization.

3. PayPal fees.
- D. Internet access
- E. Advertising
 1. Web site design and hosting fees.
- F. Medical insurance
 1. Self-employed can deduct 100% as an adjustment to gross income.
 2. Consider health savings accounts (HSAs)
 - a) Combine a high-deductible health policy with a savings account.
 - b) Use funds in the account to pay uninsured medical costs on a tax-free basis.
- G. Employee costs
 1. Compensation
 2. Insurance (e.g., workers' compensation).
 3. Employment taxes (e.g., FICA and FUTA taxes and state unemployment insurance).
- H. One-half of self-employment tax if you are self-employed.
- I. Resources
 1. IRS publications: Publication 334, *Tax Guide for Small Business* and Publication 535, *Business Expenses*.
 2. *J.K. Lasser's Small Business Taxes* by Barbara Weltman.