SALES TAX, PAYROLL TAX AND STAYING CURRENT

The taxes many small businesses collect or owe during the year, when they're due, and what happens if you fall behind.

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AT A GLANCE

- **Sales tax:** if you sell taxable products or services, you usually collect sales tax from customers and send it to your state or local government.
- **Payroll taxes:** if you have employees, you withhold some taxes from their pay and pay others yourself.
- **Estimated taxes:** owners often pay income tax in installments during the year, not just at tax time.
- Money you collect or withhold for taxes **isn't yours**. Falling behind brings penalties, and in some cases owners can be held personally responsible.

WATCH OUT

Tax rules differ by state, city and country and change often. This guide gives general US information only. Confirm your rules with your state tax agency and a tax professional.

Why it matters

Tax problems are one of the most common ways small businesses get into serious trouble. And lenders and investors check that your taxes are current before they say yes. The Project Underdogs main-street graduation standard asks for sales and payroll taxes to be paid up to date.

Sales tax

- **Who:** businesses selling taxable goods, and in some states certain services.
- **How:** register with your state for a **seller's permit** before you start selling. Collect tax at the sale, keep it separate, and file returns on schedule (monthly, quarterly or yearly, depending on your sales).
- **Online sales:** if you sell into other states, you may have to collect their sales tax once your sales there pass certain amounts.

TIP

Move collected sales tax into a separate account as soon as it comes in, so you never spend it by accident.

Payroll taxes

If you have employees, you generally:

Tax	Who pays	General rule
Federal income tax	Withheld from employee pay	Based on the employee's W-4 form
Social Security	Employee and employer	6.2% each, up to a yearly wage limit
Medicare	Employee and employer	1.45% each
Federal unemployment (FUTA)	Employer	Paid on a set amount of each employee's wages
State income and unemployment taxes	Varies by state	Check your state

Payroll taxes are usually deposited on a set schedule and reported quarterly. Most small businesses use a **payroll service** to handle it. See **O-03 Payroll Basics**.

> KEY POINT
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> Taxes withheld from employees are held "in trust" for the government. If they aren't paid, the IRS can hold the owners or others responsible for paying them **personally**.

Estimated taxes for owners

If you're a sole proprietor, partner or LLC owner, taxes usually aren't withheld from your earnings. You may need to pay **quarterly estimated taxes**. Federal due dates are generally around **April 15, June 15, September 15 and January 15**. You'll also owe **self-employment tax** (Social Security and Medicare for the self-employed), which is generally 15.3% on most of your net earnings.

Step by step: staying current

1. **List every tax you owe or collect.** Ask a tax professional to review the list.
2. **Register** for any permits or accounts you need.
3. **Put every due date on a calendar.** See **O-13 Compliance Calendar**.
4. **Set money aside** as you earn it, in separate accounts.
5. **File and pay on time,** even if you can only pay part. Late filing penalties are often larger than late payment penalties.
6. **If you fall behind, act fast.** Talk to a tax professional and ask the agency about payment plans.

> EXAMPLE
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> Mei started selling candles at markets without a seller's permit. When she found out, she registered with her state, filed for the months she'd missed with a tax preparer's help, and paid the tax she should have collected. Now she moves 7% of every sale into a "sales tax" account and files quarterly.

Common mistakes

- **Spending collected sales tax.** It belongs to the state.
- **Paying workers as contractors when they're really employees.** It can lead to back taxes and penalties. See **O-02 Employees vs. Contractors**.
- **Ignoring estimated taxes** until April, then owing a large bill plus penalties.
- **Not opening letters from tax agencies.** Respond quickly. Problems grow when ignored.

Your checklist

- ☐ Find out if what you sell is taxable in your state
- ☐ Register for a seller's permit if needed
- ☐ Set up a payroll service before your first hire
- ☐ Ask a tax professional about quarterly estimated taxes
- ☐ Put every tax due date on your calendar
- ☐ Open separate accounts for sales tax and income tax savings

Key words, explained

Word	What it means
Seller's permit	State registration that lets you collect sales tax.
Withholding	Taxes taken out of an employee's paycheck.
FICA	Social Security and Medicare taxes.
Self-employment tax	Social Security and Medicare tax for people who work for themselves.
Estimated taxes	Tax payments made during the year.

Where to go next

- **B-14 Business Taxes: What You Owe and When**
- **O-03 Payroll Basics**
- **O-13 Compliance Calendar**

IMPORTANT
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