

SAMPLE PAGES FROM

TAX RETURN ANALYSIS:

**ESSENTIALS &  
1040 REVIEW**

Linda Keith, CPA

PO Box 1366

OLYMPIA, WA 98507

360.455.1569

[WWW.LINDAKEITHCPA.COM](http://WWW.LINDAKEITHCPA.COM)

[WWW.LENDERSONLINETRAINING.COM](http://WWW.LENDERSONLINETRAINING.COM)

Use this sheet to write down the bright ideas you get in the workshop or as you review the manual. What questions do you need to ask a senior lender or look up in loan policy? What adjustments does your company not make that you think are a good idea and should be proposed? Any questions about your company's guidelines? When you get back to the office or finish your review of the manual, turn to this page and pursue these items...**NOW!**

- [illegible]

# 1-3 Linda Keith, CPA Tools and Resources

**Linda Keith, CPA, CSP** works with banks and credit unions and their lenders, underwriters and analysts to say "Yes" to good loans.

Linda is known as the CPA who likes to play. Making the right loan decision is serious business. But there is no reason not to have some fun while learning about it. People learn better when having fun.

## EXPERIENCE

- Public Accounting and Tax Practice
- Training lenders since 1986
- Open-enrollment workshops
- Onsite training
- Real Estate investor
- Commercial borrower many times over for family owned construction company
- Invited by the Central Bank of Russia to present on business lending in 1994

## CREDENTIALS

- Certified Public Accountant
- Certified Speaking Professional...the highest earned designation from the National Speakers Association, the premier professional association of independent keynoters and trainers in the country. Only 8 CPAs have earned this designation.

## EXCEL-BASED GLOBAL WORKSHEETS

Excel-based because we all know how to use Excel™, Linda's worksheets walk you through the process of tax return analysis.

- Includes built in help boxes
- Easy to review the work of others or yourself
- Flexible to fit your guidelines or approach
- Excellent and consistent documentation

## VIRTUAL TRAINING

Join a virtual class which combines self-study online modules with live webinars and an active online discussion group over the four-week session.

[WWW.LENDERSONLINETRAINING.COM](http://WWW.LENDERSONLINETRAINING.COM).

## ONLINE SELF-STUDY

Access self-study online modules at

[WWW.LENDERSONLINETRAINING.COM](http://WWW.LENDERSONLINETRAINING.COM).

- Short, concise, convenient and practical (each is 30 minutes or less)
- Take the modules before, after or as an alternative to 'live training'
- Includes additional topics Linda cannot fit into the live-training agenda
- Fast-paced, interactive, colorful...just like Linda!

[WWW.LINDAKEITHCPA.COM](http://WWW.LINDAKEITHCPA.COM)

Also found at our website....

- [Ask Linda Blog](#)
- [Contact us to ask your own questions!](#)

**Please note:** This publication is designed to provide accurate and authoritative information in regard to the subject covered. It is sold with the understanding that the author is not engaged in rendering legal or accounting services. Do not use this manual as a substitute for adequate training or consultations with professional advisors, when necessary.

Policies and procedures vary. Consult the policies and procedures of your company or a senior lender before making adjustments recommended here.

---

"The manuals are a great tool!"  
Travis Schieffer, LPO, Dakota Mac  
For more information or to order the manual, [click here](#)

Sections in **Blue** Are Included In This Sample

## **SECTION 1: INTRODUCTION**

<b>Welcome</b> .....	1-6
<b>Basic Approach</b> .....	1-8
<b>Variations on the methods</b> .....	1-9
<b>What to Look For: The Six Ns</b> .....	1-10
<b>Suggested Procedure for Cashflow Analysis</b> .....	1-12
<b>Loan Request Checklist</b> .....	1-14
<b>Copyright Notice</b> .....	1-18
<b>Cashflow Worksheets with help notes</b> .....	1-19

## **SECTION 2: FORMS AND EXPLANATIONS**

<b>Sample Tax Return Explanation</b> .....	2-2
<b>Cashflow Worksheets</b> .....	2-3
<b>Key to icons</b> .....	2-9
<b>Form 1040, Page One</b> .....	2-10
<b>Form W-2, Wages</b> .....	2-12
<b>Form 1040, Page Two</b> .....	2-14
<b>Schedule A: Itemized Deductions</b> .....	2-16
<b>Schedule B: Interest and Dividends</b> .....	2-18
<b>Schedule C: Profit or Loss from Business</b> .....	2-22
Basics List .....	2-23
Overview List .....	2-23
Cashflow the Schedule C .....	2-24
Line-by-Line Notes .....	2-24
Advertising: Line 8 .....	2-24
Car & Truck: Line 9 .....	2-24
Depreciation: Line 13 .....	2-24
Insurance: Line 15 .....	2-24
Interest: Line 16 .....	2-25
Legal and professional services: Line 17 .....	2-25
Pension and profit sharing: Line 19 .....	2-25
Repairs and maintenance: Line 21 .....	2-25
Taxes and Licenses: Line 23 .....	2-25
Disallowed Meals: Line 24b .....	2-25
Wages: Line 26 .....	2-25
<b>Schedule C, Page two</b> .....	2-26
Other Expenses: Line 27 .....	2-27
Home office deduction: Line 30 .....	2-27
<b>Summary of Schedule C Analysis</b> .....	2-29

<b>Schedule D: Capital Gains &amp; Losses, Page One .....</b>	<b>2-30</b>
Noncash items .....	2-31
Lines 4 and 11: Undistributed, Like-Kind, Installment .....	2-31
Line 13 Capital Gain Distributions.....	2-31
Gains/Losses from Stock and Real Estate .....	2-32
Active Traders: Stock .....	2-32
Active Traders: Real Estate.....	2-32
Sell-Off: Stock.....	2-33
Sell-Off: Real Estate .....	2-33
<b>Form 8949: Sales &amp; Other Disposition of Capital Assets .....</b>	<b>2-35</b>
<b>Schedule E, Page One: Rentals .....</b>	<b>2-36</b>
<b>Schedule E: Partnerships, S Corporations, Estates, Trusts.....</b>	<b>2-38</b>
<b>Schedule F: Profit or Loss from Farming .....</b>	<b>2-40</b>
<b>Form 4562: Depreciation.....</b>	<b>2-42</b>
<b>Form 4684: Business Casualty Losses.....</b>	<b>2-46</b>
<b>Form 4797: Sales of Business Property .....</b>	<b>2-48</b>
<b>Form 6252: Installment Sale Income.....</b>	<b>2-50</b>
<b>Form 8582: Passive Loss Activity.....</b>	<b>2-52</b>
<b>Form 8824: Like-Kind Exchanges .....</b>	<b>2-54</b>
<b>Form 8829: Home Office .....</b>	<b>2-56</b>
<i>Form 8949: Sales &amp; Other Disposition of Capital Assets (See 2-35)</i>	
<b>Asking Questions .....</b>	<b>2-58</b>
<b>Schedule C worksheet Completed .....</b>	<b>2-60</b>
<b>Rentals worksheet Completed.....</b>	<b>2-62</b>
<b>Completed Worksheets .....</b>	<b>2-63</b>
<b>Next steps.....</b>	<b>2-64</b>

## SECTION 3: CASE STUDY DRILLER RETURN

## SECTION 4: CASE STUDY FLINTSTONE RETURN

## SECTION 5: SOLUTIONS

## SECTION 6: THE END

Cashflow Worksheets .....	6-3
Excel Worksheets Instructions .....	6-13
Index .....	6-15

“Excellent reference material.”

Andrea Martin, Cascade Bank

Digital manuals are part of our Online Training. [Click here for more information.](#)

You have chosen to invest time in gaining the full use of an important loan-qualifying tool. You may be sitting in a workshop, taking the online modules or studying this manual on your own.

**YOU WILL** increase your competence and confidence in making loan decisions when you are lending to a business or your borrower has income from self-employment, rentals, RE contracts or capital gains.

**YOU WILL** be able to create stronger relationships with your borrowers by

- more informed discussion
- more targeted questions
- saying "yes" to good loans

**YOU WILL** gain information and practice skills that will help you personally move forward in your job and career.

### **I PROMISE YOU IT WILL BE A WISE INVESTMENT.**

Lenders attending this workshop or using this manual tend to have a wide variety of previous training and experience. It will be helpful for you to set a goal that is appropriate for your background. Take a moment to consider your starting point.

- How long have you been in lending?
- What type of training have you had on tax return analysis?
- Do you analyze tax returns currently?
- Do you use tax returns daily? ...once a week? ...once a month?
- Is your focus consumer, real estate or commercial lending?

Having answered those questions set yourself a realistic goal. If you are relatively new to tax return analysis or you use it very infrequently, your goal may be exposure to what is possible and mastery of the basic procedure and approach. You will need to use the manual as a continuing resource and refer to it often.

Because I target the workshop/manual to work for a range of lender experiences, there may be some specific comments or references that you don't quite understand. Don't let that throw you.

On the other hand, if you have been in lending for quite some time or you use tax returns daily your goal will be to fill in the gaps and better understand what you already know from experience. You would expect to pick up on more, if not all, of the specific tips, traps and recommendations.

By setting a realistic goal for yourself, you can get the most from the information provided. You can move the farthest distance from your starting point. For many of you attending the presentation it will be a stretch.

**There is no one way to do tax analysis. Be sure to consult with written policies/guidelines, a senior lender or underwriter before applying any specifics you learn here.** It is not my place to change your financial institution's procedure or policies. Those guidelines have been chosen based on risk culture and other factors. Between my information and your hard work, we will increase your ability to understand and use tax returns, whatever your system.





**MY GOAL IS:**



The Worksheets automatically do the math and carry numbers forward from rental, sole proprietorship, corporation and partnership worksheets. You still make the judgment calls.

For more information or to order the manual, [click here](#)

The two most common approaches have variations.

### **ADJUSTMENT (AGI) METHOD:**

In the adjustment method, start with the bottom line of the tax return. I call this 'tax return income' but the official label is **Adjusted Gross Income (AGI)** on a 1040, **Ordinary Income** on a Partnership or S Corporation return and **Taxable Income** (before NOL and Special Deductions) on a Corporate Return. Some lenders start with 'Total income' on the 1040.

Then review the return to make adjustments to this bookkeeping/tax number to get to **recurring cashflow available to pay debt and/or the owners**.

### **SCHEDULE ANALYSIS (S/A) METHOD:**

In this method, you build cashflow item-by-item. You look at each source of income and decide if you will include it and/or if it needs adjustment before including it. You also look for items that may not be on the return or legitimately not fully reported.

### **ADVANTAGES OF ADJUSTMENT (AGI) METHOD:**

With the AGI method, I think it is easier to review the work of a junior lender. You can easily see what adjustments have been made and summarize the difference between the number the borrower gave you, taxable income (AGI), and the number you are using in your qualifying income calculations.

It also is easier to self-review. I look at my starting number and try to put into a couple of sentences the main reasons why it is different than the recurring cashflow I am crediting to the borrower.

### **ADVANTAGES OF SCHEDULE ANALYSIS METHOD:**

This method is more intuitive to me. You end up with a list of cashflow sources you expect. The completed worksheet gives you a snapshot of borrower cashflow.

### **EITHER WAY:**

You need to review relevant, material items in a return and know what items may not be there that have impact on cashflow. You need to decide what to include and not to include in recurring cashflow.

### **AgLending MIXED APPROACH**

In AgLending, the worksheet often starts with a very detailed list of all farming revenue sources and expense categories to facilitate comparing the operation from one year to the next.

Depreciation (sometimes called use cost) is entered on a line the system will add back to come up with debt repayment capacity.

Also, some credit officers need to carefully distinguish between term debt interest and operating line interest if their system handles them differently.

The non-farm section has less detail.

### **HISTORICAL AND/OR RECURRING CASHFLOW**

We all need to get to recurring cashflow to make a good loan decision. Consumer and mortgage lenders often do this in one pass of the 1040, leaving out nonrecurring income like the occasional capital gain from a stock sale. They usually average the 'recurring' cashflow from the most recent two or three years.

Business and commercial real estate lenders often prefer a two-step method. They may do a historical/actual cashflow analysis of two or three years first. What did happen in the checkbook?

Once they have a good understanding of what has been happening with cashflow, they are in a better position to project the future cashflow.

On page 10, the types of adjustments are separated into historical and recurring to accommodate either approach.

### **PROJECTED CASHFLOW**

I distinguish between recurring cashflow and projected cashflow, although you may use the terms differently.

For me, recurring cashflow is based on known information. Perhaps the borrower just received the last payment on a note receivable. Or they may have sold a rental. We can document this.

In my mind, projected cashflow comes into play when a business is starting, expanding or changing in



a significant way. It is based on guessing, hopefully educated guessing. Assessing projected cashflow is beyond the scope of this manual. We will focus on historical and recurring cashflow.

### DEBT-TO-INCOME RATIO

This ratio is used to evaluate personal loans or the strength of a business guarantor. The personal annual debt payments are divided by the net cashflows from all sources including wages, investments, rentals and self-employment.

Debt payments related to business or rentals are generally subtracted from business or rental income rather than included in personal debt.

Debt-to-Income ratios typically range from 35% to 50% if using before-tax cashflow or 45% to 60% if using after-tax cashflow.

Some financial institutions use a sliding scale. The higher the income, the greater debt-to-income ratio they allow.

### NET SPENDABLE

Instead of using a debt-to-income ratio, some lenders subtract a family living expense based on number in the family and perhaps the income level. Then they either subtract debt (the answer needs to be positive) or they divide the result by debt from all activities (see debt-coverage ratio below.)

### DEBT-SERVICE OR DEBT-COVERAGE RATIO

The income before interest deductions is divided by the annual debt payments. We add back the interest wherever we find it and enter the corresponding debt on the debt list.

A debt-service ratio of 1.2 to 1.3 is often required. Sometimes the ratio can be lower if the residual (after-debt) income is higher. Your guidelines may provide for a sliding scale.

With a closely held business, the debt figure used often includes personal, rental and business debt. (See 'Global Cashflow' on this page.)

Commercial lenders subtract owner withdrawals, dividends or distributions to owners to determine how

much cashflow was left in the business to cover the business debt payments.

### BEFORE-TAX VERSUS AFTER-TAX

When analyzing business owner's returns, before-tax figures give you an equivalent to gross wages in a debt-to-income ratio approach. In my experience, before-tax is used by most consumer/mortgage lenders and perhaps half of business lenders.

When using a before-tax approach, and assuming a 40% debt-to-income ratio, the taxes are covered by the other 60% of income along with food, clothing and other expenses.

The debt-to-income ratio allowed is greater when using an after-tax income figure — perhaps 45% - 60% instead of 35% - 50%.

If you will be using after-tax figures, consider whether the income or self-employment tax should be adjusted for nonrecurring income/expenses or optional expenses you are adding back. If the income changes the taxes will change.

An NOL that has just been used up will no longer shelter income from taxes, also requiring an adjustment to taxes. (See more on NOLs on page 11.)

### GLOBAL CASHFLOW

Lenders commonly look at the business and the owners as if they were one entity. The owners control what they pay themselves. By combining the analysis, the lender considers the strength of both the business and the owner/guarantors.

A common technique is to analyze the business and each guarantor separately adding back interest when you find it. Often on the personal analysis for each family an amount for family living is subtracted. Then the combined cashflow available to pay debt from the business and all guarantors is compared to the combined debt from them all.

Usually we are looking for a minimum debt coverage ratio and perhaps a minimum level of overall liquidity.

---

"The workbook is user friendly."

Susan Castillo, Loan Officer, Bank of Walnut Creek

Digital manuals are part of our Online Training. [Click here for more information.](#)

## HISTORICAL OR RECURRING ...

<b>NONTAXED</b> income/gain	<b>NONDEDUCTED</b> expense/loss	<b>NONCASH</b> income or expense
Missing pieces Income not taxed	Missing pieces Expenses not deducted	Tax-impact items that do not represent cash in or out
<b>Income examples:</b> <ul style="list-style-type: none"> <li>• Child support rec'd</li> <li>• Tax-exempt interest</li> <li>• Non-taxed portion of SS, IRA, pension</li> </ul>		<b>Income examples:</b> <ul style="list-style-type: none"> <li>• IRA Rollovers</li> <li>• Roth IRA Conversions</li> <li>• Pass-thru K-1 income/gains</li> </ul>
	<b>Expense examples:</b> <ul style="list-style-type: none"> <li>• Principal loan payments</li> <li>• 50% meals/entertainment</li> </ul>	<b>Expense examples:</b> <ul style="list-style-type: none"> <li>• Depreciation, amortization, depletion</li> <li>• Carryovers</li> <li>• Net Operating Loss (NOL)</li> <li>• Pass-thru K-1 expense/loss</li> </ul>
<b>AGI Method:</b> <ul style="list-style-type: none"> <li>• Add (Gross up?)</li> </ul>	<b>AGI Method:</b> <ul style="list-style-type: none"> <li>• Add back interest and subtract full debt or put on debt list</li> <li>• Subtract 50% meals</li> </ul>	<b>AGI Method:</b> <ul style="list-style-type: none"> <li>• Subtract noncash income/gains if increased AGI</li> <li>• Add back noncash expenses/losses if reduced AGI</li> </ul>
<b>S/A Method:</b> <ul style="list-style-type: none"> <li>• Add (Gross up?)</li> </ul>	<b>S/A Method:</b> <ul style="list-style-type: none"> <li>• Add back interest and subtract full debt or put on debt list</li> <li>• Subtract 50% meals</li> </ul>	<b>S/A Method:</b> <ul style="list-style-type: none"> <li>• Only subtract noncash income or add back non-cash expenses if they have impacted a number you are using in cashflow such as Schedule C Net Profit</li> </ul>

**GROSS UP NONTAXED INCOME**

If you subtract federal income taxes do not use this idea.

This is a common technique to get all income included at its taxable equivalent. This is **ONLY** needed when you use a before-tax approach and your guidelines assume all income is taxed.

If you are not sure if your company allows this adjustment, ask first.

Consistently applied to child support, tax-exempt interest, untaxed disability/social security/pension and IRAs, you multiply nontaxed income by 1.25 which brings it up to taxable income if the borrower is in a 20% bracket. Other factors:

- 1.2 factor is 15% bracket
- 1.6 factor is 39% bracket
- Or calculate:  $1/(1-\text{tax rate})$

## RECURRING (CONTINUED) ...

NEW income/expense	NONRECURRING income/expense	NONDOCUMENTED income
Missing pieces New since tax return year	They received it or spent it but we don't think it will continue	Income you do not need to qualify which would require additional documentation
<b>Income examples:</b> <ul style="list-style-type: none"> <li>• New rental</li> <li>• New job</li> <li>• New business contract</li> </ul>	<b>Income examples:</b> <ul style="list-style-type: none"> <li>• Alimony (maybe)</li> <li>• Contract receivable (maybe)</li> </ul>	<b>Income examples:</b> <ul style="list-style-type: none"> <li>• Alimony received (maybe)</li> <li>• Contract receivable (maybe)</li> </ul>
<b>Expense examples:</b> <ul style="list-style-type: none"> <li>• New lease</li> <li>• New alimony payments</li> </ul>	<b>Expense examples:</b> <ul style="list-style-type: none"> <li>• Moving expense</li> <li>• Disaster repairs</li> <li>• Merger costs</li> </ul>	
<b>AGI Method:</b> <ul style="list-style-type: none"> <li>• Document first, then add income and subtract expenses</li> </ul>	<b>AGI Method:</b> <ul style="list-style-type: none"> <li>• Add back expenses and subtract income</li> </ul>	<b>AGI Method:</b> <ul style="list-style-type: none"> <li>• Subtract non-documented income</li> <li>• Make note of this potential additional source of income</li> </ul>
<b>S/A Method:</b> <ul style="list-style-type: none"> <li>• Document first, then add income and subtract expenses</li> </ul>	<b>S/A Method:</b> <ul style="list-style-type: none"> <li>• Add back expenses and subtract income if included in a figure you are using for cashflow such as Schedule C Net Profit</li> <li>• Otherwise, do not include</li> </ul>	<b>S/A Method:</b> <ul style="list-style-type: none"> <li>• Subtract if it is included in a number you are using in cashflow such as Schedule C Net Profit</li> <li>• Otherwise, do not include</li> <li>• Make note in comments</li> </ul>

## NET OPERATING LOSS

These are carryforwards of losses related to business, work, casualty or theft. NOLs may be pass-throughs from a partnership or S corporation. They can be carried forward 15-20 years.

They are always noncash and in a 1040 are found on Page One, Line 21.

**A statement showing the year it came from, how much was used each year and what is left is required.**

If there is remaining NOL to carryforward, this may be a compensating factor. To the extent the borrower has an NOL, they are not paying taxes on some of their otherwise taxable income.

## Suggested Procedure for Cashflow Analysis

This procedure will assist the lender in keeping track; help document the thought process, questions and judgment calls; provide a tool for selling the loan recommendation and enable senior lenders to evaluate.

### 1. ALWAYS USE A WORKSHEET!

**2. PROCEED LINE-BY-LINE** through the first page of the Form 1040. When you come to a line that is carried forward from another Form or Schedule, circle the number and go find it on its supporting schedule. Circle the number when you find it and be sure it is the number you are looking for. This ensures you have all of the schedules that support the front page of the return. Proceed line-by-line down that schedule, then return to the page from which you came.

**3. FOR EACH ENTRY ON THE RETURN** your choices are:

#### AGI METHOD

- no adjustment necessary.
- adjustment necessary and can be determined with information available, enter on appropriate line of the cashflow worksheet.
- adjustment cannot be determined from information available or need additional documentation, enter on question sheet.

#### SCHEDULE ANALYSIS METHOD

- include in cashflow, enter on worksheet.
- do not include in cashflow, enter a zero on worksheet and explain.
- need additional information or documentation, enter on question sheet.
- if business or rental schedule, use bottom-line income and see AGI method.

**4. AFTER EACH FORM OR SCHEDULE** has been reviewed take a look at the cashflow worksheet section for that form to see that you have considered all important items. Then put a check mark at the bottom of that page on the tax return and return to the source schedule or form.

**5. IF THE TAXPAYER HAS INCOME** FROM A CONTROLLED CORPORATION, PARTNERSHIP OR S CORPORATION and you are doing a personal analysis, use the 1040 as the master tax return and handle each source entity as it feeds into the 1040 (on the wage line for Corporations and Schedule E, Page 2 for Partnerships and S Corporations).

**6. CONTINUE THROUGH PAGE TWO** of Form 1040. (See page 15 for what to look for on the second page of the 1040).

When you are to the bottom of page two you should have reviewed every relevant page of the tax return. Confirm this by flipping through the pages and looking for your check mark at the bottom of each.

There are some pages that are not relevant to your cashflow analysis and will not have checkmarks on them. These include Alternative Minimum Tax forms and some additional schedules the preparer may include such as detailed equipment/depreciation lists.

**7. RUN THE NUMBERS** of what you have so far and assumptions on the questions for the borrower. If there is no way they can qualify you may have enough information to decline the loan at this step. If they qualify already then perhaps you don't need to ask all of the questions you had in mind.

**8. RESOLVE QUESTIONS** for the borrower, another lender or underwriter. Note the date and time you spoke with that person. If you are not confident of the questions you have for the borrower, run them by another lender first.

If you now decide that some of the questions you wrote down as you went are not needed, remove the questions or indicate they are not material. Do not leave unanswered questions in the file.

**9. MAKE ADDITIONAL ENTRIES** in the worksheet if the answer you received from the borrower warrants it. **SHOW ALL CALCULATIONS!**

**10. NOW ADD UP THE NUMBERS.** Do they qualify?

**11. IF YOU HAVE TO MAKE A JUDGMENT CALL** calculate cashflow using the most conservative assumption.

Your guidelines may allow you to pursue the question only if it makes a difference in whether the borrower will qualify. If you choose not to pursue a significant adjustment because it is not needed to qualify, make note of it in case you need it later or it should be considered in a future loan request.

Make a note where you will notice it, however: "IF MORE QUALIFYING INCOME IS NEEDED..."

---

"Your manual is a great learning tool!"

William Meyerchak, Senior Analyst, National Bank of CA  
Digital manuals are part of our Online Training. [Click here for more information.](#)

SAMPLE PAGES FROM

TAX RETURN ANALYSIS:

**ESSENTIALS &  
1040 REVIEW**

Forms & Explanations  
Fashion Tax Return

○ = Overview

B+ = Basic and whether to add (+) or subtract (-)

# = Page in Section 2 for more on this item

# SCHEDULE C (Form 1040)

Department of the Treasury  
Internal Revenue Service (99)

## Profit or Loss From Business (Sole Proprietorship)

► Information about Schedule C and its separate instructions is at [www.irs.gov/schedulec](http://www.irs.gov/schedulec).

► Attach to Form 1040, 1040NR, or 1041; partnerships generally must file Form 1065.

Name of proprietor Imin Fashion	Social security number (SSN) 123-45-6789
A Principal business or profession, including product or service (see instructions) Retail Clothing Store	B Enter code from instructions 4   4   8   1   2   0
C Business name. If no separate business name, leave blank. Milady Fashions	D Employer ID number (EIN), (see instr.)
E Business address (including suite or room no.) ► 725 North St City, town or post office, state, and ZIP code Lacey, WA 98507	
F Accounting method: (1) <input checked="" type="checkbox"/> Cash (2) <input type="checkbox"/> Accrual (3) <input type="checkbox"/> Other (specify) ►	
G Did you "materially participate" in the operation of this business during 2016? If "No," see instructions for limit on losses . . . . .	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
H If you started or acquired this business during 2016, check here . . . . .	<input type="checkbox"/>
I Did you make any payments in 2016 that would require you to file Form(s) 1099? (see instructions) . . . . .	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
J If "Yes," did you or will you file required Forms 1099? . . . . .	<input type="checkbox"/> Yes <input type="checkbox"/> No

### Part I Income

1 Gross receipts or sales. See instructions for line 1 and check the box if this income was reported to you on Form W-2 and the "Statutory employee" box on that form was checked . . . . .	1	○ 427,742.
2 Returns and allowances . . . . .	2	1,442.
3 Subtract line 2 from line 1 . . . . .	3	426,300.
4 Cost of goods sold (from line 42) . . . . .	4	239,349.
5 <b>Gross profit.</b> Subtract line 4 from line 3 . . . . .	5	186,951.
6 Other income, including federal and state gasoline or fuel tax credit or refund (see instructions) . . . . .	6	
7 <b>Gross income.</b> Add lines 5 and 6 . . . . .	7	186,951.

### Part II Expenses. Enter expenses for business use of your home **only** on line 30.

8 Advertising . . . . .	8	24	3,500.	18 Office expense (see instructions)	18	975.
9 Car and truck expenses (see instructions). . . . .	9	24	2,250.	19 Pension and profit-sharing plans . . . . .	19	25
10 Commissions and fees . . . . .	10			20 Rent or lease (see instructions):		
11 Contract labor (see instructions)	11			a Vehicles, machinery, and equipment	20a	
12 Depletion . . . . .	12			b Other business property . . . . .	20b	○ 36,000.
13 Depreciation and section 179 expense deduction (not included in Part III) (see instructions). . . . .	13	42	24	21 Repairs and maintenance . . . . .	21	25
			5,727.	22 Supplies (not included in Part III)	22	1,776.
14 Employee benefit programs (other than on line 19) . . . . .	14			23 Taxes and licenses . . . . .	23	25
15 Insurance (other than health)	15	24	2,400.	24 Travel, meals, and entertainment		
16 Interest:				a Travel . . . . .	24a	
a Mortgage (paid to banks, etc.)	16a	25		b Deductible meals and entertainment (see instructions) . . . . .	24b	B- 460.
b Other . . . . .	16b		2,633.	25 Utilities . . . . .	25	3,570.
17 Legal and professional services	17	25		26 Wages (less employment credit)	26	○ 59,050.
				27a Other expenses (from line 48) . . . . .	27a	26 27 15,951.
28 <b>Total expenses</b> before expenses for business use of home. Add lines 8 through 27a . . . . .	28		144,353.	b <b>Reserved for future use</b> . . . . .	27b	
29 Tentative profit or (loss). Subtract line 28 from line 7 . . . . .	29		42,598.			
30 Expenses for business use of your home. Do not report these expenses elsewhere. Attach Form 8829 unless using the simplified method (see instructions). <b>Simplified method filers only:</b> enter the total square footage of: (a) your home: _____ and (b) the part of your home used for business: _____. Use the Simplified Method Worksheet in the instructions to figure the amount to enter on line 30 . . . . .	30					B+
31 <b>Net profit or (loss).</b> Subtract line 30 from line 29. • If a profit, enter on both <b>Form 1040, line 12</b> (or <b>Form 1040NR, line 13</b> ) and on <b>Schedule SE, line 2</b> . (If you checked the box on line 1, see instructions). Estates and trusts, enter on <b>Form 1041, line 3</b> . • If a loss, you <b>must</b> go to line 32.	31		42,598.			

"The materials are extremely easy to follow and very helpful."

Jennifer Kelley, Bank Officer, First Bank

For more information or to order the manual, [click here](#)



On Page One of the 1040 you'll find Business Income: Line 12. You should have circled the \$42,598 on page one and detoured here.

Circle the \$42,598 on Schedule C when you find it. If the total at the bottom of Schedule C is different, look for more Schedules C.

**BASICS** Significant source of repayment/risk?  
If not, here are the basics:

- 13** Add back depreciation.
- 16** Add back interest. 1) Subtract debt for net cash flows or 2) Put on debt list for debt coverage or 3) Fanniemaë: No debt adjustment but do not include business debt on personal list. Interest on vehicle debt may be included on Line 9 but generally is on Line 16.
- 24b** Subtract disallowed meals.
- 30** Add back home office.

### Watch For

Don't count business debt against them twice, on business and personal list.

### Overview

If you are doing a commercial loan to this company or a personal analysis where this is a significant cashflow source, this overview list can give you a good feel for the business. Spot significant nonrecurring items, fraud or an important change in the business.

**Name/** Who is the sole proprietor?

**A/** Type of Business

**C/** Look for LLC after name, indicates limited liability.

**F/** Accounting method. [If cash basis, you cannot easily compare the two years. A change in revenues could be caused by the timing of customer's payments near year-end rather than a declining or growing business.]

### Watch For

Dropping taxable business income could be caused by the timing of receipts in a cash-basis borrower or depreciation on purchase of new equipment.

**1/** Gross receipts

**11/** Part of the workforce although paid as independent contractors

**13/** If an equipment list is included, look at type and amount of equipment and whether the age of the equipment seems consistent with an ongoing healthy business of this type.

### Watch For

Watch for sell-off of equipment that is critical to operations of the business.

**16/** You need a debt list from the borrower. You may already have this clearly identified on their application.

### Watch For

Sole Proprietors regularly mix personal debt and business debt on their application.

**20b/** The business pays this to the landlord for rent. It can give you an idea of the size of space they are in.

**26/** This and Line 37 give an idea of the number of employees in addition to the owner. Consider if other family members are working without payment.

### To Do

Both methods: Enter Borrower Name, Prepared by, Business name and type, and Year on the Sole Proprietorship Schedule C Worksheet.

**S/A Method** enter Line 31 Net Profit from Schedule C.

**AGI Method** do not enter Net Profit already in AGI.

Turn the page for Line-by-Line notes on calculating the cashflow from Schedule C.



## Like what you see?

[Order](#) the full manual here.

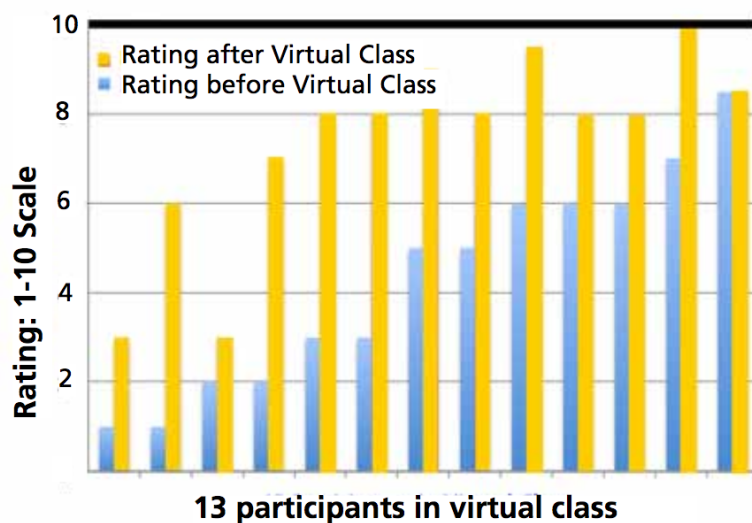
## Need more than the manuals?

Online training offers the flexibility you need to fit it into your already busy schedule, and the manuals are included at no extra charge.

## How effective is the training?

**Average Percentage Increase**

**31%**



### Participant rating:

The graph displays the self-rating of a virtual class of 13 participants on their competence and confidence in tax return analysis. The average improvement was 31%.

### Participant feedback:

- The pace is good.
- It forms a good basis for analysis.
- I have a much better understanding.
- I find myself spotting red flags and asking important questions.
- Interactive modules, quizzes and case studies helped me gain in depth knowledge.
- You opened my eyes to additional cashflow.
- Training in small chunks doesn't get boring.

Want to know more? [Click here](#) for more on our online training.

---

"The resources provided will be well-worn before too long!"

Brandon Howard, RBC Bank

Digital manuals are part of our Online Training. [Click here for more information.](#)