

Cosmetology

Learning The Art of Doing Business



*Federal Taxation Curriculum
for Cosmetology Students*

Instructor's Guide

Developed by the Internal Revenue Service

Training Goals and Principles

The training program has been structured to meet the needs of the current environment. Our primary goal is to give the student a better understanding of the tax responsibilities related to their chosen profession. This diverse industry covers a multitude of occupations such as barber, hair stylist, manicurist, masseuse, esthetician, and more.

To accomplish our goal, we have designed the chapters contained in this document to provide a basic knowledge of tax guidelines. The material is organized for maximum flexibility for use in a variety of educational settings and instructional situations.

In our continuing efforts to promote equality of opportunity for all, we ask that when conveying the materials we have provided that you, as the instructor, exercise care in the manner in which you communicate. We caution you not to exclude any one group or individual by what you do or say. As an instructor, you should avoid practices and remarks that may cause personal offense to students based on their:

- Sexual orientation
- Physical handicap
- Racial or ethnic origin
- Religious affiliation (or lack thereof)
- Age

Course Design

This course is designed to provide students with an overview of tax responsibilities. It will inform and enhance awareness of the guidelines for employees, self-employed, and employers. This course does not provide the students with information on completing a tax return. The students will have an overall understanding of the tax requirements for the Cosmetology Industry.

The exercises in the course material are designed to lead students to:

- Think about concepts
- Support facts
- Use reference materials

Any additional exercises should follow this pattern.

The instructor guide is divided into two columns: "Content of Lesson" and "Notes to Instructor." The "Content of Lesson" segment is designed to provide guidance on the information contained in each chapter. The "Notes to Instructor" segment offers suggestions to assist the instructor in teaching each chapter.

Additional exercises have been provided to further enhance understanding of the overall curriculum. These exercises may be administered during class or in independent study sessions as time permits.

Introduction

This curriculum is designed to educate students pursuing a career in the Cosmetology Industry. It consists of an overview of federal income and employment tax responsibilities.

What benefits do I receive when I file a correct tax return?

There are numerous reasons to file a correct tax return; however, we will focus on five:

- Increases chances of getting a loan
- Determines the amount of Social Security paid to your account
- Unemployment compensation is based on the amount of wages and tips reported on the federal tax return for employees
- Workers' compensation is also based on the amount of wages and tips reported
- Other benefits include life insurance, disability insurance, and retirement plans that are affected by the reported wages and tips

Reading Assignment: Have students read from "How does filing a correct tax return increase my chances of getting a loan?" to "What is my 'worker classification'?"

Ask the students to give additional reasons for filing correct returns.

What is my "worker classification"?

Choosing a career in the Cosmetology Industry offers a variety of employment opportunities. A person can be an employee, self-employed, or both.

An employee means to be employed by someone else.

A self-employed person is someone who does not have an employer. They work for themselves.

Reading Assignment: Have students read from "What is my 'worker classification'?" to "Am I an employee?"

Discuss the different types of worker classification categories.

Ask these questions:

Question: What are the different worker classifications?

Answer:

- 1. Employee*
- 2. Salon owner*
- 3. Booth renters*
- 4. Independent Contractors*

Question: A person who is a booth renter, could they be self-employed?

Answer: Yes, if they are not employees, then they are considered self-employed.

Question: Can the owner of a salon be an employee of their business?

Answer: No, generally salon owners are self-employed.

Am I an employee?

Advise students that Publication 1779, Independent Contractor or Employee, is available for more information on this topic.

Discuss the factors that determine the classification.

Reading Assignment: Have students read from "Am I an employee?" to "What is income and how do I report it?"

What is income and how do I report it?

Income is wages, salaries, tips, fees, commissions, rent, and sales. Income can be paid by cash, check, credit card or bartering. All income is taxable unless the Internal Revenue Code specifically excludes the income.

Review the examples for each category.

Reading Assignment: Have students read from "What is income and how do I report it?" to "Why are my tips considered income?"

Review the table of income.

Ask these questions:

Determine if the income has been received:

Question: A booth renter pays the salon owner rent. Was income received by the salon owner?

Answer: Yes

Question: A client gives an extra \$15 above the cost of the service. Was income earned?

Answer: Yes

your salon to pay you the amount they borrowed. Is the amount borrowed income to you?

Answer: No, the amount borrowed is not income because it was not paid to an employee or for services performed.

Why are my tips considered income?

Tip income is taxable income that is more than the amount charged for services rendered.

Tips can be paid by cash, check, charge, or by non-cash (i.e., tickets to sporting events). All tips are subject to income tax.

Tip income is reported differently for students, employees, and self-employed persons.

Reading Assignment: Have students read from "Why are my tips considered income?" to "What is a business expense and how do I report it?"

Discuss with the students the requirements for reporting tip income to employer.

Provide students with Publication 1244, Employee's Daily Record of Tips and Report to Employer.

Review the Form 4070A, Employee's Daily Report of Tips.

Review the chart that lists common types of income.

What is a business expense and where do I report it?

Business expense is an amount spent to operate the business. The expense must be ordinary and necessary to be deductible.

What do I need to know about keeping records?

Keeping good records will help in preparing an income tax return and for establishing a budget.

Have the students answer the following questions:

Question: If I am a student and receive a tip of \$30, do I need to report this to my employer?

Answer: No, a student is not an employee of the school; therefore, the \$30 is income and is reported on Form 1040, as other income.

Question: I own a salon and perform services in the salon, where do I report tip income received from clients?

Answer: Report the income on Schedule C because the owner is considered self-employed.

Reading Assignment: Have students read from "What is a business expense and how do I report it?" to "What do I need to know about keeping records?"

There are five reasons to keep good records:

1. To monitor the success of the business
2. To properly identify the sources of income
3. To properly identify deductible expenses
4. To accurately prepare the tax return
5. To support income, expenses, and credits reported on the tax return

Reading Assignment: Have students read from "What do I need to know about keeping records?" to "What are the consequences of filing an incorrect tax return?"

What are the consequences of filing an incorrect tax return?

The tax law requires that federal tax returns are to be filed by specific dates and the related taxes are to be paid by specific dates. If the required returns are not filed and/or the appropriate taxes are not paid, the IRS may assess the person with one or more penalties and interest, as appropriate.

Reading Assignment: Have students read from "What are the consequences of filing an incorrect tax return?" to "What are my tax responsibilities?"

What are my tax responsibilities?

The tax system is a pay-as-you-go system.

The worker classification will determine the taxes that need to be filed and when those taxes must be paid.

What are my federal tax responsibilities as an employee?

Employees will have income and Social Security taxes withheld from their pay. They will receive a Form W-2 from the employer showing the amount of federal taxes withheld and paid throughout the year. If an employee does not report all of the tips they received to the employer, then the employee will be required to pay additional tax. In addition, a penalty may be assessed if the employee underpays the required tax.

What are my personal federal tax responsibilities if I am self-employed?

Self-employed persons are responsible for paying their own taxes. They will pay self-employment tax, which is similar to Social Security and Medicare Taxes, but a different rate.

For the self-employed, discuss the Form 1099-MISC, Miscellaneous Income

What are my federal tax responsibilities if I am an employer?

An employer is responsible for employment taxes. Employment taxes consist of employee's federal income tax; Social Security and Medicare Taxes, the employer's share of Social Security and Medicare Taxes, and possibly, federal unemployment tax.

The employer is required to provide employees with Form W-2. Form 1099-MISC is required if the employer paid \$600 or more to any person (other than a corporation) who is not an employee.

Ask the following questions:

Question: An employee's income received for the year should be reported by the employer on which form?

Answer: Form W-2

Question: Would a self-employed person receive a Form W-2 for services performed in their salon?

Answer: No, Form W-2s are only issued to employees.

What are tax credits?

There are several tax credits a person can take on their tax return that will reduce the amount of tax owed. This section will discuss one of the tax credits, the Earned Income Tax Credit (EITC).

To be eligible to receive EITC, a person must meet several qualifications.

Reading Assignment: Have students read from "What are tax credits?" to "What are education credits?"

Review the qualifications for the Earned Income Tax Credit.

What are education credits?

There are two kinds of education credits students may be entitled to take to reduce the amount of tax owed.

Review the rules for the Hope Credit and the Lifetime Learning Credit.

Students may be eligible for both tax credits; however, they can only claim one.

Reading Assignment: Have students read from "What are education credits?" to "What is e-filing?"

Refer the students to Publication 970, Tax Benefits for Higher Education.

What is e-filing?

A person may file their federal tax return electronically. e-filing is accurate, secure, and paperless. Individuals, self-employed, employers, partnerships, and tax practitioners can use e-file.

Reading Assignment: Have students read from "What is e-filing?" to "What is EFTPS?"

Advise the students of the tax forms that can be used to e-file.

What is EFTPS?

The Electronic Federal Tax Payment System (EFTPS) allows individuals, self-employed persons, employers, and corporations to pay their federal taxes electronically. Any individual taxpayer making more than one tax payment a year can use EFTPS. Any business taxpayer can use EFTPS for all taxes.

Reading Assignment: Have students read from "What is EFTPS?" to "Test Your Knowledge."

Review the benefits of using EFTPS.

Related Products and Services

Review the list of products and services.

Test Your Knowledge

Have students complete additional questions.

Review and discuss answers.

Additional Exercises:

1. Linda decided to open *Your Special Beauty Salon*. She hired Kathy, Lisa, and Danny to work in her salon. Kathy and Lisa recently graduated from Cosmetology School. Linda provided them with a contract that stated the hours they would work and information on health insurance and tip reporting. Danny rented a booth from Linda. He buys his own supplies and sets his own hours and fees. Determine if Kathy, Lisa, or Danny are employees or self-employed.

Answer: Kathy _____

Lisa _____

Danny _____

2. Determine who must report tip income to their employer.

- _____ a. Marcus provided service and received \$75 of which \$5 was tip income for the month of June.
- _____ b. Wilma earned \$22 in tips last week.
- _____ c. Jessica, a student at the National Cosmetology School, received \$20 in tips from a client.
- _____ d. John worked four days and received tips of \$150

3. Circle the best answer. When should an employee report tip income to the employer?

- a. 1st of every month
- b. 10th of every month
- c. 15th of the following month after the tips are earned
- d. 10th of the following month after the tips are earned

4. Circle the best answer. Determine which of the following are business expenses.

- a. A \$300 neon sign with the business' name on it.
- b. Electric bills for the business.
- c. Purchased laundry soap to be used to wash children's clothes.
- d. Shampoos and hair curlers.
- e. Trade association dues.

5. Match the following:

- | | |
|---|--|
| <input type="checkbox"/> Form W-2 | a. Used to report income and expenses from self-employment. |
| <input type="checkbox"/> Form W-4 | b. Used to report \$600 or more to any person (not a corporation) for services rendered. |
| <input type="checkbox"/> Form 2106 | c. Used to report employees wages. |
| <input type="checkbox"/> Schedule C | d. Used to report employee business expense. |
| <input type="checkbox"/> Form 4070A | e. Used to determine the amount of income tax to be withheld. |
| <input type="checkbox"/> Form 1099-MISC | f. Used to report employee's daily tips. |

6. True or False. A 20 year-old student who does not have children can qualify for the Earned Income Tax Credit.

7. What are the two kinds of education credits that a person may take on their tax return?

- a. School and Learning Credit
- b. Higher Education and Lifetime Credit
- c. Hope and Scholarship Credit
- d. Hope and Lifetime Learning Credit

8. Alex is a full-time student at Dean Beauty College. Alex paid for his tuition, books, and lab fees that cost \$3,200. He cannot be claimed on his parents' return. This is his first year of school, and he has met all the requirements. Can Alex claim the Hope Credit?

Yes No

9. List at least three types of people who can file electronically.

10. Can EFTPS be used to file a tax return?

Yes No

Answers to Additional Questions

1. Kathy employee
Lisa employee
Danny self-employed
2. b, d
3. d
4. a, b, d, e
5. c Form W-2
e Form W-4
d Form 2106
a Schedule C
f Form 4070A
b Form 1099-MISC
6. False, a person must be at least 25 years old to be eligible.
7. d
8. Yes
9. Individual taxpayers
Sole proprietors
Employers
Partnerships
Tax practitioners
10. No. EFTPS is used to make payments and not for filing a return.



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