Entrepreneur

The 2 Glaring Mistakes Entrepreneurs Make When It Comes to Taxes

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Q: What is the biggest mistake entrepreneurs make when it comes to taxes?

A: Often entrepreneurs make their biggest tax mistakes before they are even up and running by overcomplicating their initial business setup.

And unfortunately, once entrepreneurs fall into this trap, they can get stuck in for a long time.

But it doesn't have to be this way. Here are a few mistakes entrepreneurs make and how to overcome these obstacles.

1. Too focused on structure and the best place to incorporate

Entrepreneurs tend to get obsessed with decisions like “What state should I incorporate in?” “Should I incorporate offshore or in the US?” and "How should I structure my business?"

Unless your business is kicking off with more money than you know what to do with and your shareholders are demanding that you “optimize your tax structure,” then follow the old KISS protocol: “Keep It Simple Stupid.” Use an LLC to limit your personal liability, keep your set up costs low and use a jurisdiction you either know a lot about (e.g. your home country) or where you can easily figure out the rules and find help when you need it.

After the structure and location is decided, the entrepreneur can reinvest all his extra time, energy and money into building his business and perfecting his product or service. And as your business grows, there will be plenty of time to change the structure if you need to, and it makes good business and financial sense!

2. Not keeping proper financial records

This is not sexy part of the job, but it is extremely important for a business to know its financial position, keep accurate records and be able to access its records.

Many entrepreneurs start their business out of their own personal bank accounts. They are focused on the first few sales, building a customer base and creating a perfect service or product. Then the tax year ends and they pull together what they have and ship it off to their accountant, or try to prep their own taxes. More often than not this turns ugly.

If you don’t properly maintain records and receipts for your sales and expenses, then you can run into a couple problems: You can over state your profits and end up with a big tax bill, miss legitimate expenses and end up with a big tax bill or fail to file the appropriate paperwork (e.g. quarterly self-employment payments) and end up with a big tax bill and penalties. You get the point. If you don't keep and maintain accurate books, then you are at risk for making financial mistakes on your taxes -- and this can be costly. And of course if you don't know where your business is financially, you are also at risk of running out of cash, selling products or services that are not profitable, overpaying suppliers, getting ripped off by bank and the list goes on. Any and all of these mistakes can lead to bankruptcy.

Fixing these mistakes

The language of business is accounting. You don't need to be an accountant to understand the language, but you do need to make an effort to understand where your business is financially on a monthly basis. The best way to do this is to get a good bookkeeper, set up on an online software and set aside time each week to review your numbers. A few best practices include:

- Involve a tax accountant early in the process, not just at year end
- Look at your P&L often to see if anything looks odd
- Think about what expenses you have coming up and make sure you budget the cash to pay for them. Don't be shy about asking your accountant or bookkeeper to explain things to you. If your accountant or bookkeeper is putting everything together for you, they should be able to answer your questions with minimal effort.
- Keep clean books. Don't fill your business with lots of personal expenses.

Time and money are invaluable to entrepreneurs starting out. It's important the initial tax decisions along with the ongoing upkeep are made wisely and efficiently in order to invest time and energy in where it matters most: the products and services. The decisions affecting your tax liability can truly make or break your company, so make sure to keep it simple and not over-complicate things.