

GENERAL TAX INFORMATION FOR INDEPENDENT CONTRACTOR PHYSICIANS

LOCUM TENENS INDUSTRY ISSUES



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GENERAL TAX INFORMATION FOR INDEPENDENT CONTRACTORS

Being a physician engaged in an independent business and profession can bring great rewards and freedoms. It also brings great responsibility to ensure compliance with the rules and requirements of the Internal Revenue Service (IRS) and other taxing authorities including state and city governments. The following information is designed to help you consider some of the tax issues you may face as a contracted physician.

FEDERAL TAX REPORTING

If you are an independent contractor physician working on a locum tenens basis with VISTA Staffing Solutions, Inc. (VISTA), you are considered a self-employed individual for tax purposes. Unlike an employee who has half of his or her Social Security and Medicare taxes paid by the employer, a self-employed person must pay his or her own Social Security and Medicare taxes. This tax is called self-employment tax. The self-employment tax rate is 15.3 percent of a self-employed individual's earnings up to the taxable limit for Social Security, which is \$87,900 for 2004. The self-employment tax rate above the Social Security limit is 2.9 percent. As a self-employed individual, you may be responsible for completing Schedule C or Schedule C-EZ, Schedule SE, and Form 1040-ES.

- You are required to report income and expenses annually on Schedule C or Schedule C-EZ and calculate your earnings subject to self-employment (SE) tax. This schedule will also be attached to your Form 1040, U.S. Individual Income Tax Return.
- If your net earnings are more than \$400 you must pay SE tax annually using Schedule SE. This schedule will be attached to your Form 1040, U.S. Individual Income Tax Return.
- If you expect to owe taxes, including self-employment tax, of \$1,000 or more when you file your return, you generally are required to make estimated tax payments. Estimated tax is the method used to pay the tax due (including SE tax) on income not subject to withholding, as is the case with independent contractors. Use Form 1040-ES to figure and pay the tax.

One consequence of being self-employed, as mentioned above, is that generally no federal or state taxes are withheld from your paychecks as they are for employees. Instead, self-employed individuals must normally pay estimated taxes directly to the IRS. You must ordinarily pay estimated tax in four installments, starting on April 15. However, no payments are due until you actually earn the income.

To figure your estimated tax, you must figure your expected adjusted gross income, taxable income, taxes, deductions, and credits for the year. When figuring your estimated tax, it may be helpful to use your income, deductions, and credits from the previous year as a starting point. You must then make adjustments for changes in your own situation for the current year. The worksheet included in Form 1040-ES and IRS Publication 505, Tax Withholding and Estimated Tax can help guide you through the process of computing estimated tax.

The IRS imposes a penalty if you underpay your estimated taxes. You must pay the taxes due plus a percentage penalty for each day your estimated taxes went unpaid. This percentage is set by the IRS each year. In recent years, the penalty has ranged from 6 percent to 8 percent annually.

The due dates and periods covered for each installment payment are shown to the right.

Visit <http://www.irs.gov/businesses/small/index.html> for more information on self-employment federal tax issues.

If you have created a professional corporation to contract with VISTA, other rules apply that are not addressed here.

Income Received for the Period	Estimated Tax Due
January 1 through March 31	April 15
April 1 through May 31	June 15
June 1 through August 31	September 15
September 1 through December 31	January 15 of next year

STATE TAX REPORTING

Along with federal tax responsibilities, self-employed individuals also have state tax responsibilities. As an independent contractor of VISTA, you may work in several states during the same year. Generally, you will be required to pay income taxes to those states for the portion of income earned in the respective state. For state tax purposes, there are generally three filing statuses to consider. You may be considered a resident, a non-resident or a part-year resident. Some states have income tax plus other types of taxes that may be due, such as local and city taxes. In addition, some states, such as California, may require an employer who has contracted with a non-resident self-employed individual to withhold taxes on amounts they may pay that individual. The states of Alaska, Florida, Nevada, New Hampshire, South Dakota, Texas, Washington, and Wyoming do not have an individual income tax and therefore require no individual income tax payment. It is important to understand your filing status for each state wherein you performed services in order to comply with the rules and regulations of that state.

Visit <http://www.statetaxcentral.com/cache/indguide.htm> for a list of common state tax issues.

Visit <http://www.taxfoundation.org/individualincometaxrates.html> for a listing of state income tax rates.

BUSINESS EXPENSES

One advantage of being self-employed is that you can deduct your eligible business expenses directly against your income; regardless of whether you itemize your deductions. You will not be subject to the 2 percent of adjusted gross income threshold that applies to an employee's out-of-pocket business related expenses. As a self-employed individual, your business expenses reduce the amount of your income that is subject to the self-employment tax while the unreimbursed business expenses of an employee do nothing to reduce the FICA tax.

To be deductible, a business expense must be: 1) directly connected with your trade or business; 2) "ordinary" (customary or accepted in the business), and 3) "necessary" (appropriate and helpful to the business; it doesn't have to be indispensable or essential, but it cannot be lavish or extravagant). In addition to these basic rules, there are strict limits on the deductibility of business-related meals, entertainment, auto, gifts and home office deductions. Some of these expenses that are likely to apply to you are:

1. **Travel expenses** incurred while away from home overnight are allowed as a business deduction. Travel expenses include meals, lodging and local transportation. Because VISTA provides air travel, lodging and local transportation, most of your travel expenses will be paid by VISTA and, therefore, non-deductible. However, you may incur other business expenses that are not paid for or reimbursed by VISTA, including meals, laundry, fees, tips, and postage. These expenses must be substantiated by the amount, time, place, and business purpose. Alternatively, the IRS has provided per diem allowances under which the amount of meals and incidental expenses may be deemed to be substantiated, thus eliminating the need for detail record keeping. The per diem rate depends on the locality of travel. Check www.gsa.gov for the latest rates.
2. **Entertainment expenses** (including business meals) must be either "Directly related" to the active conduct of business or "Associated" with business. "Directly related" to the active conduct of business occurs where business is the primary purpose of the meal or entertainment. Generally, this test is not met if the event occurs in a setting where there is little or no possibility of conducting business, such as night clubs, theaters, or sporting events. The active conduct of business requirement means more than a general expectation of a specific business benefit at an indefinite future time. "Associated" with business occurs where the meal or entertainment directly precedes or follows a substantial business discussion (which business discussion is part of an active effort to obtain a specific business benefit), and the business discussion is the principal purpose of the event. It is not necessary that more time be devoted to business than entertainment.

Other business expenses may include:

- Commissions
- Computer expenses
- Education expenses for yourself
- Insurance (may exclude life and disability insurance)
- Interest expense
- Legal and professional fees (accounting fees)
- Pension and profit sharing contributions
- Qualified home office, if eligible
- Rent or lease expenses
- Repairs
- Subscriptions to professional trade and technical journals
- Supplies and materials
- Tax and licenses
- Tax preparation fees
- Telephone

No deductions are allowed for entertainment facilities (yachts, hunting lodges, swimming pools, tennis courts, or bowling alleys). If you meet all of these tests, generally, only 50 percent of business entertainment is deductible.

3. **Automobile Expenses** directly attributable to the conduct of business are deductible. One exception is commuting expenses, which are defined as travel between a taxpayer's residence and a regular business location within the area of the taxpayer's residence. Travel, however between a taxpayer's residence and a temporary work location can be deducted. A temporary work location is defined as work location where the taxpayer does not anticipate working more than one year. Being self-employed, generally all miles traveled for business are considered deductible.

Once an auto is determined to qualify for business, the deduction must be calculated, one of two ways: 1) actual expenses (gas, repairs, insurance, etc.) plus depreciation, or alternatively, 2) the standard mileage allowance may be used (36 cents/mile for 2003 and 37.5 cents/mile for 2004). Depreciation is already built into the standard rate; no depreciation is allowed for cars for which the standard rate is chosen. For those electing actual expenses, only the business percentage may be depreciated. If the car is used 75 percent for business use, only 75 percent of the cost may be depreciated. Depreciation and lease expenses are also subject to limits based on the cost and value of the car. All automobile expenses must be separated by those attributable to business use and those attributable to personal use. Only the portion attributable to business use is deductible.

4. **Clothing** is not deductible, unless it has a permanently affixed logo (uniforms) and/or is used solely for business purposes and would be conceived as such. A lab coat, for example, would be considered a deductible clothing expense; however comfortable walking shoes would not. Also, cleaning and laundering clothing that would be considered deductible is also a valid business expense.

An IRS Form 1099-Misc will be issued to all independent contractor locum tenens physicians for compensation paid. The amount on the 1099 will not include payments for substantiated reimbursed expenses or expenses paid to a third party on behalf of the independent contractor and therefore should not be deducted on the independent contractor's personal income tax return.

It is very important that self-employed individuals keep a record of their business expenses. Proper recordkeeping is vital to substantiate business deductions. You must have evidence of business use. An IRS auditor can deny any expense if you don't have proof of each expenditure, showing the date, the amount, and the business purpose.

The preceding information was prepared for VISTA Staffing Solutions, Inc., by CBIZ FPG Business Services, Inc. to provide independent contractor locum tenens physicians a general overview of possible tax ramifications of working as an independent contractor. It is important that you consult your tax advisor to receive more detailed information relating to your personal situation. Information is based on tax law in effect as of January 1, 2004. The information contained herein should not be used in any actual transaction without the advice and guidance of an appropriate professional tax advisor who is familiar with all relevant facts, since some issues may be subject to differing interpretations. The information contained herein is general in nature and is not intended, and should not be construed as legal or tax advice or opinion provided by CBIZ FPG Business Services, Inc. or VISTA Staffing Solutions, Inc. to the reader. The reader is also cautioned that this material may not be applicable to, or suitable for, the reader's specific circumstances or needs and may require consideration of other matters (including financial and tax factors) if any action is to be contemplated. Neither CBIZ FPG Business Services, Inc. nor VISTA Staffing Solutions, Inc. assumes any obligation to inform the reader of any changes in the tax law or other factors that could affect the information contained herein.

Some other useful resources addressing some of these tax issues include the following:

1. IRS Publication 334, Tax Guide for Small Business
2. IRS Publication 463, Travel, Entertainment, Gift and Car Expenses
3. IRS Publication 505, Tax Withholding and Estimated Tax
4. IRS Publication 533, Self Employment Tax
5. IRS Publication 535, Business Expenses
6. IRS Publication 1779, Employee/Independent Contractor Brochure
7. IRS Topic 554, Self Employment Tax
8. IRS Topic 408, Sole Proprietorship

VISTA Staffing Solutions, Inc., shall have no responsibility for the filing of any physician's income tax. Each independent contractor locum tenens physician who contracts for placements through VISTA Staffing Solutions, Inc., is solely responsible to meet all reporting and paying requirements as it relates to federal, state, and any other taxing authority.