

Filing a 1040 for a “gig” worker with a full-time job¹

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ABSTRACT

Chad Wilt sighed as he began sorting through his business expenses in preparation for doing his 2020 taxes. He wondered aloud if he would even qualify for any itemized deduction after a dismal business year for his consulting practice. COVID-19 had taken a toll on his clients' businesses and that meant they weren't hiring Chad's business, EliteConsulting, LLC, for leadership training or executive coaching. Chad felt like he was at a career crossroads. He enjoyed the balance of a full-time position coupled with a consulting side gig but now wasn't sure if the side gig would work out. He knew he had some hard decisions to make but he wanted to hold off until after he had filed his 2020 taxes and had a thorough analysis of his business. Since it was already the last week of March 2021, Chad had to collect his business documents and hand them off to his tax preparer. For the 2019 filing, Chad had to make further payments of \$1,952 to the IRS and \$3,174 to the Ohio Treasurer of State. He was very eager to know how much he might be paying for 2020. Although Chad knew which forms and schedules would need to be attached to his Form 1040 from the previous work of his tax preparer, he never had a complete understanding of the purposes of them. To avoid unintentional negligence and misrepresentation of the information about his income and expenses, like other small business owners, Chad had his professional tax-preparer take care of the filing for him. At this point, he just wanted to see if he could benefit by changing his tax filing option. He would wait on his big decision of whether to close his consulting business.

Keywords: Form 1040, federal tax filing, deduction, Schedule C, married filing separately

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¹ This is a decision case. All information (except those with sources specifically quoted) used in this case were obtained and/or confirmed from the protagonist whose identity was disguised. The names of the individual, the firms/organizations and the locations, as well as some key numeric information, were also modified (where necessary) to protect the privacy of the protagonist and the confidentiality of his information. The case describes a situation where a college professor with a side consulting gig had to file his 1040 taxes. His tax filing would be used to make other business decisions for his consulting practice. This case looks into the income generation of the individual Chad Wilt amid a pandemic, the corresponding tax filing, followed by the consideration/decision of whether to change his tax filing options in order to gain the most benefits. Teaching notes to this case are available. For those instructors who are interested in obtaining them, please contact Oi Lin Cheung at ocheung@iue.edu.

INTRODUCTION

Chad Wilt sighed as he began sorting through his business expenses in preparation for doing his 2020 taxes. His consulting practice, EliteConsulting, LLC, had generated an income of \$27,621 in 2018 and \$14,962 in 2019. He wondered aloud if he would even qualify for any itemized deduction (IRS, 2021a) after a dismal business year for his practice. COVID-19 had taken a toll on his clients' businesses and that meant they were not hiring EliteConsulting for leadership training or executive coaching. He enjoyed the balance of a full-time position coupled with a consulting side gig but now, after a hard year, he was not sure if it was worth holding on to his consulting business. He knew he had some hard decisions to make but he wanted to hold off until after he had filed his 2020 taxes and had a thorough analysis of his business. Chad had to collect his business documents and hand them off to his tax preparer soon so he could evaluate his situation and make some hard decisions. He was hoping that the Schedule C of his 1040 filing would help him make some strategic decisions. For now, he just wanted to focus on his tax filing so he had the data needed for his subsequent decision-making.

CHAD WILT AND HIS BUSINESS

Chad remarried and had a son from his previous marriage. His son was grown and out of the house. Recently he and his wife were thrilled to welcome twin grandsons to the family. He was working as an assistant professor in business for a large university in Lansing, Michigan. His five-year tenure clock would "officially" end in September 2021 when his promotion and tenure dossier would be due. He had an annual three-three course load with summer teaching assignments. All his courses had been delivered face-to-face until the COVID-19 global pandemic hit in March 2020. He was then forced to deliver all his courses online. And, due to COVID-19, he was approved, upon his request, with an extension of one year to his tenure clock, giving him until September 2022 to submit his dossier. As all his courses were running online, he worked from home beginning in March 2020 for his professor job.

At the same time, Chad owned and operated a small consulting business, EliteConsulting, LLC, specializing in executive coaching, leadership training, and strategic planning. The business was established in 2008. Most of his consulting work was delivered on-site at the offices of his clients. Many executive coaching sessions were held during lunch or breakfast time at a local restaurant, affording his clients the opportunity to both eat and avoid constant interruption by coworkers and direct reports. Moreover, Chad did not hire any employees. He liked the agility of being a sole proprietor. Thus, he had conducted his business at his home located in Toledo, Ohio since the establishment of EliteConsulting. At times, he even invited his clients to his home office to work together there to brainstorm ideas or work out business challenges on Chad's big whiteboards he had installed in his home office. Since Chad used space in his home to operate his business, he claimed a home office deduction on his taxes (IRS, 2021c). He also traveled in his own vehicle back and forth between his home and the locations where he met with his clients. Therefore, he was eligible to claim a similar vehicle use deduction on his taxes as well (IRS, 2021f).

INCOME AND EXPENSES FOR 2020

Chad's W2 Wage and Tax Statement for 2020 from Rainbow State University (see Figure 1(a)) indicated that the taxable amount of compensation he earned from the university for the year was \$90,230.82. This was also the amount of earnings the university paid him, subject to social security tax as well as Medicare tax. Although these three amounts were the same, the federal income tax withheld, social security tax withheld and the Medicare tax withheld were different: \$16,490.24, \$5,594.31, and \$1,308.35 respectively. While Chad's federal tax withholding was based on his tax filing status and the number of allowances he claimed (IRS, 2021e), his amounts of withholding for Social Security tax and Medicare tax were determined according to their current tax rates. The Social Security tax for 2020 was at the same 6.2% for employees and employers. On the other hand, the 2020 Medicare tax on both was 1.45% (IRS, 2021g). In addition, his employer-sponsored health coverage amounted to \$26,475.30 but it was not taxable. While Chad was not required to pay the Michigan state tax, his income of \$90,230.82 was still subject to local tax which amounted to \$451.15, being 0.5% for a non-resident working in Lansing (Michigan Department of Treasure, 2021).

Chad also did some consulting work for Innovative Life Coaching (a small life coaching organization) that required him to be an employee of the organization in 2020. He delivered a couple of short training sessions on how to establish a consulting practice to individuals seeking a life coaching accreditation. Chad considered this work to be consulting work even though it produced a W2 (see Figure 1 (b)). He was not salaried or paid by hourly wages for this job. Instead, he was paid a flat rate of \$6,000 per training session. The life coaching organization was then purchased by a venture capital group in April 2020 and Chad's services and employment/consulting ended early in the year.

Chad's Form 1099-INT Interest Income illustrated that he earned \$253.63 on a bond investment in 2020. He paid \$1,672 interest on his student loan balance (a loan he obtained for paying the tuition in order to earn a doctoral degree for his professor job) as indicated in his Form 1098-E Student Loan Interest Statement. He refinanced his home mortgage, which was originally obtained from Ohio Mortgage Corp., with Homeowner Financing, Inc. when he married his current wife in July of the year. Thus, he paid a combined mortgage interest amount of \$5,680 (being \$3,857 to OMC and \$1,823 to HF) in 2020.

Chad and his wife were living in a 4,025-square foot home which called for an annual real estate tax of \$4,751 and an annual homeowner association (HOA) fee of \$200. His home office where he conducted his business for EliteConsulting was 402 square feet large. He had a 2017 Ford Fusion, which he bought in September 2016 for \$36,750. It was for both his business and personal uses. He started using the vehicle largely for his business from the beginning of 2017. He estimated that he had driven it for 6,873 miles for running his EliteConsulting business during 2020. For these miles, he would be able to claim a deduction of 57.5¢ per mile (see Table 3). Since his wife worked as a lawyer, they each owned a vehicle for their own uses. She drove a 2018 Jeep Grand Cherokee. Chad used an app called MileIQ to track all his personal and business miles. He would not have a problem furnishing the information to the IRS if requested for auditing purposes.

Figure 1. An Excerpt of Chad’s W2s for 2020
(a) From Rainbow State University

a Employee's social security number 789-12-3456		OMB No. 1545-0008		Safe, accurate, FAST! Use  Visit the IRS website at www.irs.gov/efile	
b Employer identification number (EIN) 99-8885533		1 Wages, tips, other compensation 90230.82		2 Federal income tax withheld 16490.24	
c Employer's name, address, and ZIP code RAINBOW STATE UNIVERSITY 1200 UNIVERSITY PARKWAY LANSING, MI 48864		3 Social security wages 90230.82		4 Social security tax withheld 5594.31	
		5 Medicare wages and tips 90230.82		6 Medicare tax withheld 1308.35	
		7 Social security tips		8 Allocated tips	
d Control number		9		10 Dependent care benefits	
e Employee's first name and initial Last name Suff. CHAD B. WILT 1562 SUNSHINE Dr, TOLEDO, OH 43606		11 Nonqualified plans		12a See instructions for box 12 DD 26475.30	
		13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input checked="" type="checkbox"/> <input type="checkbox"/>		12b	
		14 Other		12c	
				12d	
f Employee's address and ZIP code		15 State Employer's state ID number MI 000998887700		16 State wages, tips, etc. 17 State income tax 18 Local wages, tips, etc. 90230.82 19 Local income tax 451.15 20 Locality name LAN	

Form **W-2 Wage and Tax Statement** **2020** Department of the Treasury—Internal Revenue Service
 Copy B—To Be Filed With Employee's FEDERAL Tax Return.
 This information is being furnished to the Internal Revenue Service.

(b) From Innovative Life Coaching

a Employee's social security number 789-12-3456		OMB No. 1545-0008		Safe, accurate, FAST! Use  Visit the IRS website at www.irs.gov/efile	
b Employer identification number (EIN) 99-7654321		1 Wages, tips, other compensation 12000.00		2 Federal income tax withheld 1941.34	
c Employer's name, address, and ZIP code INNOVATIVE LIFE COACHING 720 INDEPENDENT ROAD TOLEDO, OH 42305		3 Social security wages 12000.00		4 Social security tax withheld 744.00	
		5 Medicare wages and tips 12000.00		6 Medicare tax withheld 174.00	
		7 Social security tips		8 Allocated tips	
d Control number		9		10 Dependent care benefits	
e Employee's first name and initial Last name Suff. CHAD B. WILT 1562 SUNSHINE DR. TOLEDO, OH 43606		11 Nonqualified plans		12a See instructions for box 12	
		13 Statutory employee Retirement plan Third-party sick pay <input type="checkbox"/> <input type="checkbox"/> <input type="checkbox"/>		12b	
		14 Other		12c	
				12d	
f Employee's address and ZIP code		15 State Employer's state ID number OH 66-0123456		16 State wages, tips, etc. 12000.00 17 State income tax 367.03 18 Local wages, tips, etc. 19 Local income tax 20 Locality name	

Form **W-2 Wage and Tax Statement** **2020** Department of the Treasury—Internal Revenue Service
 Copy B—To Be Filed With Employee's FEDERAL Tax Return.
 This information is being furnished to the Internal Revenue Service.

(Chad Wilt, personal communication, May 25, 2021)

Table 1. Chad's Selected Expenses for 2020

Expense	Total Amount	Proportion Eligible for Counting toward EliteConsulting	Amount Applied to EliteConsulting
Real Estate Taxes	\$4,751	10%	\$475
Annual Homeowner Association Fee	\$200	10%	\$20
Palmer Energy (Electricity and Gas)	\$4,400	10%	\$440
Toledo Water Distribution (Water)	\$640	10%	\$64
Waste Management (Trash)	\$350	10%	\$35
Verizon (Cell Phone)	\$743	50%	\$372
Frontier (Cable)	\$2,304	50%	\$1,152
Entertainment: Meals	\$3,080	50%	\$1,540
Total	\$16,468		\$4,098

(Chad Wilt, personal communication, May 25, 2021)

His home-related expenses were allocated pro-rata to EliteConsulting in accordance with the proportion of his home office size in his total home square footage (IRS, 2020c). During an unofficial consultation offered by an IRS employee, Chad (who was also classified as self-employed with respect to his business) learned that he was eligible to claim 50% of his costs on meals, cell phone, and cable as business expenses to EliteConsulting (Yavorski, 2020). Since Chad's customers were both local and regional, his mileage and entertainment expenses could vary from year to year. During 2020, much of his consulting transitioned to online delivery and his ability to network, entertain and attend conferences also fell significantly.

Chad made several donations during 2020 to churches and charitable organizations. The total amount and distribution of the donations can be seen in Table 2. All donations except the one made to Goodwill were in cash. Chad donated to Goodwill various household items he purchased over time. Those items were expected to have an aggregate fair market value of \$783 as estimated at the time of donation. Chad used the guidelines provided by Goodwill to estimate the fair market value of items donated.

Table 2. Charity Donations Over 2020

Organization	Amount
Trinity Church	\$245
Holy Spirit Church	\$5,900
Grace House	\$600
Faith International	\$675
Goodwill Industries	\$783 (fair market value)
Total	\$8,203

(Chad Wilt, personal communication, May 25, 2021)

Chad's 2019 income was over the maximum income to receive the payments for the coronavirus stimulus checks (Peter and Peterson Foundation, 2021). His Form 1095-C Proof of Insurance indicated that he had employer-provided health insurance offer and coverage through 2020, which was a requirement for large employers under the Affordable Care Act, or Obamacare (Turbotax, 2021).

Although EliteConsulting (with the North American Industry Classification System (NAICS) code 541600) was founded as a limited liability company (LLC), it was filed as a sole proprietorship for tax purposes (IRS, 2021d). EliteConsulting's profits (and losses) were passed onto Chad's personal income as required in the Form 1040 U.S. Individual Income Tax Return. Since Chad was considered self-employed with regard to his business, thus, he had to pay self-employment taxes (both the employer and employee portions) towards Medicare and Social Security (CommunityTax, 2021) based on EliteConsulting's Income. During 2020, the business generated a total income of \$20,600 and incurred total expenses of \$12,074 (see Table 1 for \$4,098 and Table 3 for \$7,976).

Chad was a keynote speaker for two organizations that year, Ohio Management Association and Proactive & Efficient Performance Group, and charged them each a small fee. He often spoke for groups at a low fee or no fee as a means to generate more business for EliteConsulting in the future. He developed and facilitated a robust leadership training program for Flexi Glass Manufacturing and billed them as classes were delivered. Due to the pandemic, Flexi Glass had limited the number of classes they had Chad deliver in 2020.

Table 3. EliteConsulting's Revenues and Expenses for 2020

Revenue	Amount	Expense	Amount
Ohio Management Association	\$400	Postage	\$133
Flexi Glass Manufacturing	\$19,600	Subs, Pubs, Dues	\$1,642
Proactive & Efficient Performance Group	\$600	Office Supplies	\$376
		Cost of Goods Sold (Assessment tool units)	\$1,573
		Mileage 6,873 @ 57.5¢/mile (The Balance, 2021)	\$3,952
		Tax preparation for 2019 filing	\$300
Total	\$20,600		\$7,976

(Chad Wilt, personal communication, May 25, 2021)

When calculating his business expenses, Chad tracked mileage, office supplies, subscriptions, office equipment, entertainment, professional services, and assessment unit costs. Chad often bought three-ring binders and three-hole punch paper in bulk as supplies for his consulting work. His office supplies expense list could also include interesting props or materials he used to reinforce key learnings or points. His home office closet held hundreds of permanent markers, craft beads, a fish bowl, poster boards, and lots of books and resource materials for organizational development best practices. Since he facilitated training sessions on leadership, Chad used several apps and tools to keep his business running smoothly, including anti-virus software, google drive space, a subscription to a legal service, a back-up software program, a

mileage tracker, as well as web hosting for a website he had not updated for a decade but felt he needed to have. For 2020, Chad had expenses for postage, subscription and related items, as well as office supplies as shown in Table 3.

As part of his business, Chad used Harrison Assessments (a commonly used assessment tool in the consulting and coaching industry) to measure work behaviors and preferences. The tool could be useful in understanding qualifications for hiring and promotion as well as development opportunities. Reports for the assessment were paid for by the unit, which could be purchased by his clients through a distributor such as EliteConsulting in a bundled offering with consulting or other intervention. The units were sometimes sold directly to his clients who administered the assessment tool themselves to evaluate their employees. When a client bought units through EliteConsulting, Chad made a profit from the sale. Thus, he treated the amount he paid Harrison for the units as the cost of goods sold to his business. Chad bought the assessment reports, as well as office supplies, to meet the needs of consulting projects of his business. Thus, those expenses varied year-over-year depending on the volume of the business.

Harrison Assessments could also be used for succession planning where the human resources department or managers evaluated the suitability of a candidate for promotion or another role in the organization. The tool identified work behaviors so it was also helpful for professional development. Chad often used the tool to narrow in on work behaviors which might be preventing an employee from performing at the highest level. The tool identified 12 paradoxical traits, for example, which could illuminate strengths and challenges in interpersonal skills, leadership behaviors, and achievement behaviors. Chad also used the tool as a team building aid where a group of employees could compare and contrast their results to better understand team dynamics. The assessment also had an applicant tracking system (ATS) embedded into its platform. The ATS allowed employers to screen job candidates using weighted measures for eligibility. Those who passed the first screening for eligibility then could take the assessment to determine if they possessed the behaviors needed for the job. The tool used analytics to predict job fit suitability and could compress the hiring cycle substantially. One of Chad's clients, Flexi Glass Manufacturing, had integrated the Harrison Assessment into several areas of its talent management system; for hiring, training, coaching, and team development.

THE 2020 INCOME TAX FILING

Chad was used to hiring a tax preparer² to do his tax filing. His tax preparer charged him \$300 to file his 2019 taxes in 2020. Due to the pandemic, the preparer did not plan on raising her service charge in 2021. Chad had chosen to file his tax return as “married filing separately.” For the 2019 tax filing, he had to make payments of \$1,952 to the IRS and \$3,174 (including a state penalty/interest of \$81 due to the underpayments of the quarterly Pass-Through Entity Tax for EliteConsulting (IRS, 2021b)) to the Ohio Treasurer of State, in accordance with the estimation of his tax preparer. Chad’s 2019 total Ohio income tax liability was \$3,864. As his business volume went down tremendously due to COVID-19, he was very eager to know whether he still needed to make any further tax payment for 2020 on top of his tax withholdings. Based on the estimation in his prior filings, Chad believed that EliteConsulting’s quarterly taxes required to be paid to IRS (IRS, 2021b) and Ohio for 2021 would approximate to \$700 and \$500 respectively. Chad had a \$2,643 Ohio state income tax return for 2019. He applied this amount fully to his

² Chad’s tax preparer was Susan Smith who ran the Smith Tax Service (EIN 666097654) located at 2306 South Third Street, Toledo, OH 43610. Her PTIN was P00099999. She could also be reached by phone at (330)947-2138.

2020 Ohio state tax payment. At the same time, he had one (1) exemption to claim in his Ohio individual income tax in the amount of \$1,900 for 2020.

Although Chad knew which forms and schedules would need to be attached to his Form 1040 from the previous work of his tax preparer, he never had a complete understanding of the purposes of them. To avoid unintentional negligence and misrepresentation of the information about his income and expenses, like other small business owners, Chad had his professional tax-preparer take care of the filing for him. He was very eager to see his Schedule C and know what his reported income was for the business. At the same time, he wanted to know if switching to filing his income tax jointly with his wife would be more beneficial to his current tax situation.

APPLICATION

The case is most applicable in courses in taxation. It could be used in an entrepreneurship or entrepreneurial finance class if the class consists of a significant number of accounting students who could lend their expertise to teams working on the case. Although it is highly recommended for use in the upper under-graduate level and/or graduate level courses, the case is a good candidate for discussion in business and/or taxation workshops as well.

LEARNING OUTCOMES

The objectives are:

1. Identify the forms and schedules for tax return filing by a small business owner
2. Discuss the basic terms and concepts used in taxation
3. Prepare the income tax filing for a small business owner
4. Compare the pros and cons in switching tax filing status

DISCUSSION QUESTIONS

1. What forms and schedules would need to be included in Chad's 2020 complete tax filing packet? Briefly explain. (LO1)
2. What were Chad's possible options for his Form 1040 filing status? Compare and contrast each of them. (LO2)
3. Why was EliteConsulting subject to the pass-through entity tax? (LO2)
4. Being both an employee and the sole owner of a small business, what were the possible exclusions and deductions applicable to Chad? Why? (LO2)
5. What would Chad's tax packet look like in his actual filing? (LO3)
6. Would Chad be better off if he switched to other possible filing options? What information would be needed to evaluate his options? (LO4)

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