



Owner-Operator Financial Handbook

A practical, common sense guide to money management for the professional driver.

Central Business Services
Owner Operator Financial Handbook

This handbook was developed by Central Business Services, Inc., a tax and financial services firm dedicated to the needs of the over the road driver. Our purpose is to provide you with financial information that will help you to become more financially successful in your career as an owner operator. Our handbook does not attempt to cover every aspect of your finances but rather focuses on those subjects that, if understood clearly and if put into practice, can make the difference in your financial success.

Experience has shown very clearly that, most often, financial problems that are experienced by drivers are not income related problems but rather they are spending related problems. Therefore, it makes sense that the more you understand about your finances the greater opportunity you have to manage your money effectively.

SECTION 1: YOUR SETTLEMENT CHECK

Without question, the most significant difference between the pay of the owner-operator and the company driver is the fact that NO TAXES AT ALL are withheld from an owner-operator's check. This is of extreme importance. Obviously, if no taxes are paid in during the year, when April 15th arrives quite likely a large balance will be due. At the end of the year, owner-operators receive a document referred to as a "1099". This is the equivalent of the employee W-2. The primary difference is that the only figure on the 1099 is your gross compensation for that tax year since no taxes have been withheld. The company is required each year to send to the IRS an original of each Form 1099 issued so that the IRS can ensure that each owner-operator claims the proper amount of income on his/her individual tax return.

A self-employed individual generally pays taxes into the IRS during the year through the Estimated Tax System.

SECTION 2: BOOKKEEPING AND TAXES

Without question, there are more tax "breaks" available for the average over the road driver than in virtually any other occupation, but in order to take advantage of these tax savings opportunities, you must know what the rules are. This section will provide a brief discussion of the major tax aspects of being a professional driver. It should be emphasized that this handbook is not a substitute for having a professional tax advisor. A good tax advisor who specializes in trucking will typically save his clients many times any fees charged.

It is likely that your tax return will be more complex than it has been for you in the past. It is very common for those in the trucking industry to have relatively complex tax returns because of the large number of out of pocket expenses that the IRS allows as tax deductions.

Effective financial management for owner-operators involves much more than just a basic understanding of taxes. Every business owner, regardless of the size of the

business must ensure that the fundamentals of financial management are done properly and those fundamentals begin with bookkeeping.

It is impossible to overemphasize the importance of good bookkeeping to the success of your business. Indeed, according to the U.S. Small Business Administration, bad bookkeeping is the single biggest reason why most new small businesses fail. Therefore, if you are truly serious about success, you must pay attention to your books and records. It makes a great deal of sense for most owner-operators to use the bookkeeping and tax services of a company that specializes in the trucking industry. After all, you have enough responsibilities on your shoulders as it is and you probably have not had the training necessary to ensure that your books are prepared properly.

The end result of the bookkeeping function is to provide the owner-operator with an accurate and timely PROFIT & LOSS STATEMENT . Your P & L is really your scorecard for your business. It shows, for a specific time period (for example the month of October, or the year 2005) what your income was and what all of your tax deductible expenses were for that period. Subtracting expenses from income shows you your Net Profit. Net profit is what all of taxation is based on and is roughly the equivalent of what your gross wages would be as an employee. Every business owner should have a P&L statement each month to be able to effectively monitor the operating costs of the business.

Once the P & L is prepared, a number of analysis tools can be applied to help you to understand the financial side of being an owner-operator. From the information on the P & L a Cost/Revenue per mile analysis can be prepared. This analysis will break down all income and expenses to a per mile basis so that you will know that every time the odometer turns over how much money you brought in, how much it cost to generate that income and what was left over for you (profit). In particular, watching your Cost Per Mile on a monthly basis can provide you with an early indicator of changing patterns in operation of your company. Knowing your Cost/Revenue per mile also allows you to know the exact profitability of each load that you haul in advance.

Secondly, from the P & L data, a breakeven analysis can be created to show the owner-operator exactly how many miles must be driven each month (or year) to be able to exactly meet all expenses. Then, any miles above that point begin to generate profit.

Again, it is important to emphasize that **ALL FINANCIAL MANAGEMENT STARTS WITH BOOKKEEPING.**

The P & L Statement is also the primary tool used to manage your taxes. First, it ensures that you are getting “credit” for the money that you spend to operate your business. Remember that all tax is based on your Net Profit not on your Gross Income. Therefore, the more tax deductible expenses that you get credit for, the lower your Net Profit and the lower your taxes.

Secondly, the P & L allows you to project approximately what your tax liability will be at year end. Remember that no taxes are being withheld from your compensation but rather you must pay your taxes directly to the IRS. This is done on a quarterly basis on April 15, June 15, Sept 15 and Jan 15 of each year. Without an accurate P & L how would you know how much to pay each quarter?

Many owner-operators are under the impression that they can simply wait until the end of the year and pay all of the tax at once. If you do that, with some minor exceptions, the IRS will charge you penalties and interest on the tax.

You should view the tax expense of owning your own business in the same manner as you view any other operating expense such as fuel, maintenance or supplies. It is simply part of the cost of being in business. However, since taxes are only paid on a quarterly basis, it takes discipline to set aside enough money each month to ensure that the money is available for your quarterly payment. The best "rule of thumb" is that Uncle Sam will get approximately 25% of your Net Profit. Therefore, if your monthly P & L indicates that, for example, for the month of October, your Net Profit was \$4,000, you should set aside \$1,000 to be ready for your next Estimated Tax payment.

YOUR TAX RETURN:

When a tax return is filed, what you are really doing is settling up with the IRS for the previous year. First, a calculation is made of the taxable income of the taxpayer taking into account all sources of income (including your business) and subtracting those exemptions and expenses that are "deductible" according to IRS rules. Then, after taxable income has been calculated, the total tax is determined. This total tax is then compared to the amount of tax that has already been paid through payroll withholdings or through quarterly estimated tax payments. If too much tax has been paid in, then a refund results. If not enough has been paid in, then the balance is due when the tax return is filed.

The single most common business mistake that most owner-operators make is ignoring their quarterly payments. Obviously, if no quarterly payments have been made then the total tax for the year is due when the tax return is filed (plus penalties and interest). If that money is not available, then the owner-operator begins to sink into debt with the IRS and, when penalties and interest are considered, it is very difficult to recover. Therefore, IT IS IMPERATIVE THAT YOU STAY ON TOP OF YOUR TAXES RIGHT FROM THE BEGINNING.

One final note regarding taxes. For the great majority of small business owners, the largest tax to be paid is not income tax, but rather SELF-EMPLOYMENT (SE) tax. SE tax is basically the same as the Social Security and Medicare tax that is withheld from an employee's paycheck, with one major exception. For an employee, a total of 7.65% of gross pay is withheld for Social Security and Medicare tax. Then, the employer must match that amount before the funds are turned over to the IRS. In other words, the total tax is 15.3%, half is paid by the employee and half is paid by the employer. As a self-

employed person, the owner-operator has no employer to share the tax and therefore must pay the full 15.3%. What makes this tax so burdensome is that the tax is assessed on the full Net Profit from your business whereas income tax is only assessed after personal exemptions and personal deductions (standard or itemized) are subtracted. It is not unusual for SE tax to be double the income tax for many owner-operators.

When making quarterly estimated tax payments, both income tax and SE tax are included in the calculation of how much to pay each quarter.

SECTION 3: BUDGETING YOUR MONEY

Any discussion of the topic of budgeting and managing your money must be based on one simple, fundamental principle; **YOU MUST SPEND LESS THAN YOU MAKE**. It is not possible to develop any level of financial stability in your life without strictly following this basic principle and, further, most money problems are a direct result of ignoring it.

With this in mind, the first step is to recognize that most money problems are spending problems, not income problems and so the solution lies understanding where your money is going and having the discipline to control it. Do you know where your money is going? Most people, of course, could tell you how much their last paycheck was for but, if asked to account for where it went, they probably could not.

At the core of managing your money successfully is the creation of a workable budget. As we all know, budgets have a bad reputation – nobody likes budgets because they first of all tell us the truth and secondly they tell us what we CAN'T do. But it doesn't have to be that way. In reality, a budget is nothing more than a game plan for your money. It tells you how you would like to spend your money and what you CAN do. One of the primary hidden benefits of budgeting is that it tends to relieve financial stress. Have you ever been really "stressed out" about something but, once you sit down and analyze what it is that is bothering you, you find that you feel more relaxed and in control once again? That is what budgeting does; it gives you control over your money.

One of the big challenges in budgeting is converting a weekly settlement check into monthly expenses. For example, if your monthly rent is \$600 you should be putting aside \$150 per week to ensure that the money is available when the rent is due. If you wait until your last paycheck of the month, but that check is only \$550, you're in trouble, right? So you begin your budget by listing what your fixed monthly expenses are and begin to allocate a portion of each paycheck to cover those expenses.

In addition to your home expenses that you have budgeted for, you must also budget for your road expenses. First, you have personal expenses for which cash must be available such as food, showers, motels, entertainment, etc. Second, cash must be available for any tractor expenses that are your responsibility such as tolls, scales, cleaning supplies, parking, etc.

Once you have determined what your monthly needs are to meet your obligations and you have determined how much is needed to meet your road expenses, you then have a basic understanding of how much cash is left to spend on extras.

There are many ways to control spending on the road but there are even more money traps to avoid. Common sense tells us to avoid impulse spending, avoid video arcades and avoid convenience stores where we are all tempted by nice to have but unnecessary items. One of the greatest money saving opportunity for over the road drivers lies in food cost. You are allowed an automatic tax deduction for your meals on the road, regardless of how much money you actually spend on food. This is referred to as a per diem, or per day deduction. The tax deduction for 2008 is based on a per diem rate of \$52, of which 80% is allowed as a tax deduction. Therefore, your daily deduction is \$41.60. Remember, you get that deduction regardless of how you buy your meals. Buy yourself a good electric cooler and small microwave (tax deductible) and, to the greatest extent possible, buy food in grocery stores not restaurants. When you do this, two things happen; first you live a healthier lifestyle eating a diet of fresh foods not fried foods and second, you dramatically reduce your food costs. The average driver buying meals in truckstop restaurants will spend approximately \$25-30 per day or \$650-750 per month. Instead, if you were to buy \$50-60 of groceries per week (a lot of food for one person!) and eat only 2-3 times per week in restaurants, your monthly food cost would be roughly \$350-400 per month. That is a **savings of over \$300 per month**, a sizable difference in anyone's budget!!!

Another area where there are money saving opportunities is in long distance telephone expense. This is, of course, an industry that is changing very rapidly so it is important to continually look for advances in technology and at the same time, reduction in rates. Be sure to compare apples to apples, taking into account not just per minute charges but also base monthly charges, surcharges, set up fees, term commitments and credit checks.

Regardless of whether you are a company driver or owner-operator it is imperative that you constantly look for ways to reduce the costs of being in the trucking industry. The bottom line is by following some of these suggestions you will keep more of the money you make.

If you are having trouble paying your bills, it may be because you are too deeply in debt – a situation many people find themselves in. We began this section by saying that you must spend less than you make. If the opposite is true for you, you may be drowning in debt. If so, what can you do?

The first step is to face up to your debts and resolve NOT to go any deeper in debt by avoiding impulse purchases and spending only what you have, not what you think you'll have in the future.

- Make a list of everything you owe and your payment schedule

- Concentrate on paying off the lowest balance first
- Then take the money you would have paid on the debt you just paid off and put that, with your regular payment, on the next lowest balance
- Continue this method until all debts are satisfied

Remember, this method will only work if you DO NOT INCUR NEW DEBT!! One last point; don't become discouraged. Unfortunately, it takes very little time to get into debt but a long time to get out. But, as the old saying goes; a journey of a thousand miles begins with one step (or something like that).

SECTION 4: PLANNING FOR YOUR FUTURE

Creating a secure financial future does not happen overnight. Rather, it is the result of taking advantage of savings opportunities throughout your career and exercising the discipline to stay with it over time. Stated simply, normal people don't get rich quick, they get rich slowly and systematically over time. Most importantly, the earlier in your life you begin to plan and save for your financial future, the earlier you will reach financial independence.

Owner-operators, because they are independent and not employees do not typically have 401(k) plans available to them. However, they do have several types of tax-deferred retirement plans to choose from.

The most common type self-employed retirement plan is the Simplified Employee Pension Plan, also known as the SEP-IRA. Under a SEP plan, a self-employed individual can contribute, on a tax-deferred basis, up to 20% of his/her net profit from business operations. The SEP plan has several advantages over other types of plans:

- Can vary the percentage of contributions each year as cash is available
- No formal reporting requirements to the IRS
- No administrative costs to establish and maintain
- Can choose the type of investment you desire (mutual funds, stocks, certificates of deposits, etc.)

You should consult your tax advisor for more information on establishing, maintaining and investing in SEP plans.

EX: 1

John Sample
Monthly & Year to Date Profit and Loss
December 2007

	<u>Dec '07</u>	<u>Jan-Dec'07</u>	<u>% of</u>
<u>Income</u>			
Income			
400-Hauling Income	<u>\$9,737.00</u>	<u>\$116,851.50</u>	<u>100.0%</u>
Total Income	\$9,737.00	\$116,851.50	100.0%
Expenses			
600-Truck Lease Payments	1,400.00	16,800.00	14.4%
601-Truck Depreciation	0	0	0.0%
602-Truck Loan Interest	0	0	0.0%
610-Insurance	478.00	5,740.00	4.9%
620-Fuel Tax, Licenses, Permits	169.00	2,030.00	1.7%
630-Damage Claims	0.00	292.00	0.3%
650-Postage/FEDX	31.00	241.00	0.3%
700-Food (per diem)	570.00	6,840.00	6.6%
710-Fuel	2,468.00	29,621.00	25.3%
730-Maintenance & Repair	576.85	6,920.85	5.9%
750-Tolls & Scales	10.00	81.00	0.1%
760-Truck Washes	62.00	311.00	0.3%
770-Phone/Fax/Qualcomm	75.00	1,046.00	0.8%
780-Motels	42.75	292.75	0.3%
790-Labor	0.00	323.00	0.3%
800-Bookkeeping & Tax Services	65.00	1040.00	0.5%
810-Laundry & Uniforms	24.25	264.25	0.3%
820-Supplies	24.62	566.42	0.3%
830-Tools & Equipment	121.50	950.10	1.2%
840-Showers	0.00	24.00	0.0%
900-Miscellaneous	<u>47.20</u>	<u>568.70</u>	<u>0.5%</u>
Total Expenses	<u>6,165.17</u>	<u>73,952.07</u>	<u>63.9%</u>
Net Profit	<u>\$3,571.83</u>	<u>\$42,899.43</u>	<u>36.1%</u>

EX: 2 **ESTIMATED TAX PROJECTIONS/COST & REVENUE PER MILE**

Prepared for:
JOHN SAMPLE
PROJECTION AS OF : June 2007

The estimated tax projections shown below are based on your year to date Net Profit from your business. The estimate assumes that you will operate your business for the remainder of the year in the same manner that you have so far this year. It is extremely important that you inform us of any significant financial changes that could affect your tax situation such as marital status, children, the purchase of business equipment, etc.

QUARTERLY ESTIMATED TAX PAYMENTS

Based upon the information available to us, the following is an estimate of your total federal and state taxes for the year and a recommended amount for you to pay as your next quarterly estimated tax payment.

Projected Profit for the Year:	\$ 41,320
Projected Self-Employment Tax	\$ 6,322
Projected Income Tax	\$ 3,744
Total Tax	\$ 10,066

You should plan to make a payment to the IRS of: **\$ 2,500** on or before 9/15/07
You should plan to make a payment to the state of **\$ 250** on or before 9/15/07

If you do not have IRS form 1040ES, or the state forms, to make these payments, please call our office and we will be happy to mail or fax you additional copies.

PLEASE NOTE: since no taxes are withheld from your earnings as an owner-operator, you are required by the IRS to make these quarterly estimated tax payments. The IRS will, under most circumstances, charge you penalties and interest if these payments are not made.

COST/REVENUE PER MILE ANALYSIS

Revenue per mile:	\$ 0.96
Cost per mile:	\$ 0.52
Profit per mile:	<u>\$ 0.44</u>

These figures reflect your year-to-date operations. By knowing these figures, you will be able to project what your profit will be on each load, helping you to make better business decisions and to forecast your cash flow.

SECTION 5: RESOURCES AND REFERENCES

Services

Central Business Services, Inc. "Tax and Financial Services for Professional Drivers"
8383 Craig St #260 Indianapolis, IN 46240 1-888-255-3939.

Small Business Administration
Office of Business Development
409 3rd St NW
Washington, DC 20416
1-800-827-5722

Consumer Credit Counseling Service
Consumer Affairs Department
8611 2nd Ave
Silver Springs, MD 20910
1-800-388-CCCS

Publications

Internal Revenue Service Publications:

Pub 17	Your Income Tax
Pub 334	Tax Guide for Small Businesses
Pub 463	Travel Expenses
Pub 505	Tax Withholding and Estimated Taxes
Pub 529	Miscellaneous Deductions
Pub 533	Self-Employment Tax
Pub 535	Business Expenses
Pub 560	Retirement Plans for Small Businesses
Pub 583	Starting a Business and Keeping Records

Profitable Trucking: A Guide for the Independent Trucker. National Accounting and Finance Council. American Trucking Associations, Inc. Aug 1994.

How to Make Money in Trucking. Overdrive Book Division. Randall Publishing. 1995.