

# SelfInformed

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*NASE Member Mike Malone has had some personal training clients for more than 20 years.*



# GETTING A LOAN WHILE SELF-EMPLOYED

By Sallie Hyman

Qualifying for personal loans when you are self-employed can be very difficult, especially in today's economic climate. Most people are looking for mortgages, either a first-time mortgage or refinancing a current mortgage. Many also seek car loans.

It was not that long ago that banks would throw money at you as you walked in the door. That has changed dramatically in the wake of the subprime mortgage scandal.

Prior to the housing crisis two popular loan options included no documentation and stated income/stated asset (low documentation) loans. These riskier loans are not offered by many lending institutions today. If they are available, the interest rates are usually quite high, making them a less appealing option. Most banks will ask for verification of stated income by requesting your Schedule C forms from at least the last two years.

## PREPARING FOR THE PROCESS

The self-employed are now faced with trying to qualify for a traditional, fully documented loan. One of the greatest hurdles facing them when trying to get that loan is the paperwork. Traditional employees can verify income with a couple of years' worth of W-2s. It requires much more diligent work on the part of the self-employed to prove their income. It is imperative to keep good records. Make sure that all large payments received are properly documented so that they will be recognized as income. Try to keep business and personal bank accounts separate. Keep copies of all tax returns so they are readily accessible.

At least two years of tax returns will be required. Some lenders will ask for a Form 4506 or 8821. Form 4506 is used to request a copy of your complete tax return directly from the IRS, thus preventing you from submitting falsified returns to the mortgage company, and costs \$39 per return. But you may be able to request Form 4506-T (limited return) for free.

Form 8821 authorizes your lender to go to any IRS office and examine the forms you designate for the years you specify. This service is free. Banks may also ask for a copy of your business license to prove that the business actually exists. Other documents often requested include a signed statement from an accountant, profit and loss statements and balance sheets.

There are some things that you can do to make yourself a more attractive candidate for lenders if you are seeking a traditional loan. Experts recommend that you:

1. Know your credit score and make sure it is high. Correct any errors and do what is necessary to maximize it.
2. Offer a large down payment. This will show that you have a vested interest in the home or vehicle and it will also help to lower the loan amount.
3. Have significant cash reserves. Maintain an emergency fund. This will show lenders that you can continue to make payments even if business drops off.
4. Pay off all other debt. Pay off credit cards, car loans, and any other debt you have. This will free up available money for mortgage payments.

5. Be in business at least two years. Most banks want to see that your business has been established for at least two years. With a failure rate of over 40 percent for small businesses, banks want to see some longevity.

Even if you have all of the documentation, the banks may still be reluctant to lend due to what appears to be a low income. Most businesses will write off as many business expenses as legally possible to reduce taxable income on tax returns. This is great for helping you not have to pay much in taxes, but can be a negative when it comes time to borrow money. Mortgage eligibility is based on net income, meaning all those business deductions actually count against the borrower.

NASE Member Dudley Dix, owner of Dix Design, in Virginia Beach, Va., found this out the hard way when trying to refinance his home. Dix started working with the bank that held his mortgage. Because his company was set up as an S-corporation, part of his salary was recorded as a distribution, and the bank would not include this as income.

“Mine is a very small business that employs only me and my wife. All of the income of the business minus expenses becomes my income. In excluding the distributions portion they halved my income and disqualified us from refinancing. They said that we could not afford to pay the new mortgage repayments, even though they were to be lower than what we were paying to them at the time and on which we had never missed a payment. They were effectively forcing us to pay higher interest rates.”

After two years of trying to work with his bank, Dix was finally able to refinance with another institution.

One exception is depreciation on business-related purchases, which can be added back into the borrower’s net income to help them qualify. For example, if you write off depreciation on a car that was purchased for the business, you can write off some depreciation, but because it is a paper loss, not a real cash loss, you can add that depreciation back into your net income. That will help to increase your overall net income.

This brings up a very important point to discuss with your tax professional if you know that you will be looking to borrow money in the near future. It may be worthwhile to not take every possible business deduction on your taxes in order to show a larger net income. You will have to pay more taxes, but it will allow you to show more income to lenders.

If you need to borrow the money now and can’t wait two or three years to show greater income, then you can consider amending past tax returns. You will have to pay taxes on the amended return, but again, it will help to show a greater net income. An accounting professional can advise you on how to do this correctly. But note that the IRS has a three-year statute of limitations on amending returns.

## FINDING THE RIGHT LENDER FOR YOU

Choosing the right lending institution will make a big difference for the self-employed. “Big-box” banks usually have a neat little computerized mortgage loan program that requires all the boxes to be checked. That may be difficult for someone who is self-employed since they do not have a W-2 to show or may have to produce extra documentation. It is likely that



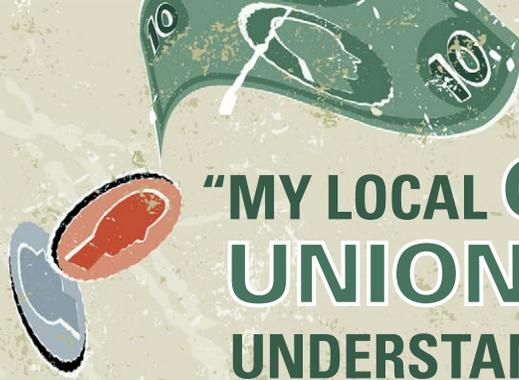
## DO YOUR RESEARCH AND READ THE FINE PRINT

NASE Business Strategy Expert Gene Fairbrother offers the following points for finding personal loans:

1. How much are you looking for and for what purpose? The amount plays an important role, because if you are looking for \$7,500 to improve your kitchen you will be looking for a different source than if you are looking for \$250,000 to buy a new home.
2. Just because you don’t qualify for a \$400,000 house or a \$60,000 vehicle doesn’t mean that you will not qualify for a \$200,000 house or a \$30,000 vehicle. Talk to a bank or other lender to get pre-qualified on how much you can borrow based on your history. You may need to lower your expectations.
3. The key components for any loan are your credit score, your credit report, your debt ratio, and your open credit available. Be sure to know all of these facts before making any application for a loan.
4. Consider peer-to-peer lending, lending clubs, or open lines of credit on your credit cards. While these might all carry a higher cost to borrow money, they are resources. Also, be cautious and carefully check the sources for anything you do online, such as peer-to-peer loans.
5. Don’t forget family and friends. While you don’t want to put them in a difficult situation, they are a common source to help out short term.
6. If you cannot get a loan to buy, consider leasing. If that loan was for a car and you don’t meet the criteria for a purchase, leasing is a good option.

7. Remember to check all the details in any loan you are looking at and read the fine print. The more difficult it is for you to find a personal loan, the more money it is going to cost you in interest rates and fees. Not knowing exactly what the real costs are could put you in a situation of paying a lot more than what the big print says.





# "MY LOCAL CREDIT UNION WAS MUCH MORE UNDERSTANDING THAN BANKS."



you will be turned down by these big banks because they are either not willing or not set up to deal with non-traditional borrowers.

It may behoove a self-employed borrower to look into smaller banks and lending institutions. Local banks with lenders that understand the area and know their customers may be a more willing option. They do not have to play by the strict rules of a large corporate bank and may be more flexible.

Credit unions are also an alternative to the big banks. They are growing in popularity as people are seeking options. These non-profit cooperatives have members who are their clients. They are still highly regulated to ensure the safety of your money, but since they are independently run, they can offer lower interest rates and fees and are able to work more with non-traditional borrowers.

NASE Member and author Skip Press, of Burbank, Calif., turned to his local credit union a few years back when he needed to refinance his vehicle. "My local credit union was much more understanding than banks. I try to 'keep local' as much as possible," says Press. Many credit unions are now offering mortgages in addition to personal loans to fill the void for those who are finding it difficult dealing with big banks.

If none of these options are viable for you, you can consider seeking a co-borrower who is a W-2 employee or finding someone who is willing to co-sign a loan for you.

Finding the right loan can take more time and effort when you are self-employed. Be prepared to meet with several lenders to get the best rate you can, have all of your documentation organized and available, and have the patience and persistence to get the job done. ■

**Sallie Hyman** writes on small-business issues and owns and operates her own small business in Purcellville, Va.



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## Ask The Experts

**Q:** *I'm about to hire my first employee and I have a few questions. Am I required to provide health insurance? Can I provide a health insurance stipend and have that qualify as providing health insurance? What is a reasonable amount to provide as a health insurance stipend?*

**A:** You are not required by law to provide health coverage to your workers because of your business size. That is your choice as the employer. You have a few options if you'd like to help your employee with health costs.

1. Determine how much you want to give them to put toward health costs and simply add it to their salary.
2. Look into setting up a defined contribution health plan for your business. As the employer, you would designate how much you will contribute to each employee's health insurance. You would then have to provide your employee(s) with insurance plan options and allow them to pick the plan that works best for them. This option is more attractive to businesses with a larger number of employees and the financial and staff resources to manage a benefit plan.
3. Set up a Health Reimbursement Arrangement (HRA) for your employee. An HRA is a written plan that allows you to reimburse your employees with a preset amount of dollars to go towards health care costs.

An HRA plan is a way to provide some financial benefit to your new worker to use towards health costs. For example, you could set up an HRA and designate \$500 per year as the amount that you can afford to reimburse to your employee for health care costs. The employee could then purchase health insurance, go to a doctor for a check-up, purchase prescriptions, visit an urgent care center, etc. As long as the cost qualifies as an **allowable medical expense** according to IRS rules, they simply bring the receipt to you and you reimburse them the cost with a company check up to the limit of \$500 that you had set. Then you get the benefit of deducting those costs as business expenses.

## GET MORE ANSWERS

The NASE's small-business experts are here to help you understand the ins and outs of operating a successful small business. And access to these professionals is free with your NASE Membership!

Just go online to the [NASE Business Learning Center](#) where you can ask the experts questions about:

- Taxes
- Marketing
- Financial issues
- Employee relations
- Accounting rules
- And much more

The experts are available 24/7 and ready to help!

One thing to note is that an HRA has non-discrimination rules, meaning that if you hire another employee, you are required to provide them with the same financial benefit noted in the HRA. You can learn more and [set up an HRA for free through the NASE's HRA 105 program](#).

As to what is a reasonable amount for you to contribute to health insurance costs of your workers, that is a decision that should be made based on the budget for your business. You can find information regarding [the cost of coverage in each state from The Kaiser Family Foundation](#).

*Kristie Arslan, NASE Health Reform Expert* ■

# Member Spotlight

## Fitness Fanatic

*Michael Malone has been an NASE Member since 2005. He owns **Fitness and Nutrition For Life** in East Greenwich, R.I. You can also find him on Twitter, @Michael\_getfit, and on Facebook.*

### Tell us about your business.

I started my business in 1990. I wanted to help people and make a difference while doing something I had a passion for. My business, Fitness and Nutrition for Life, provides personal training, nutrition plans, post-rehab conditioning, life fitness coaching, assessments, and martial arts and kickboxing for individuals, groups, schools, and corporations. I recently launched my website, [fitnessandnutritionforlife.com](http://fitnessandnutritionforlife.com), a completely mobile website for clients on the go with HD-quality videos of fitness programs, nutrition plans, and fitness and nutrition tips.

### What's your favorite thing about your business?

One of my favorite things about my business is that I can positively impact the lives of others through improved fitness and nutrition. I've been doing this for three decades, and I've learned so much by teaching others. But, seeing my clients (some of whom I've worked with for 20 years) improve their physical lives is just a part of what I do. The discipline of proper training and a healthy lifestyle will always improve a person's emotional life and relationships with others and themselves.

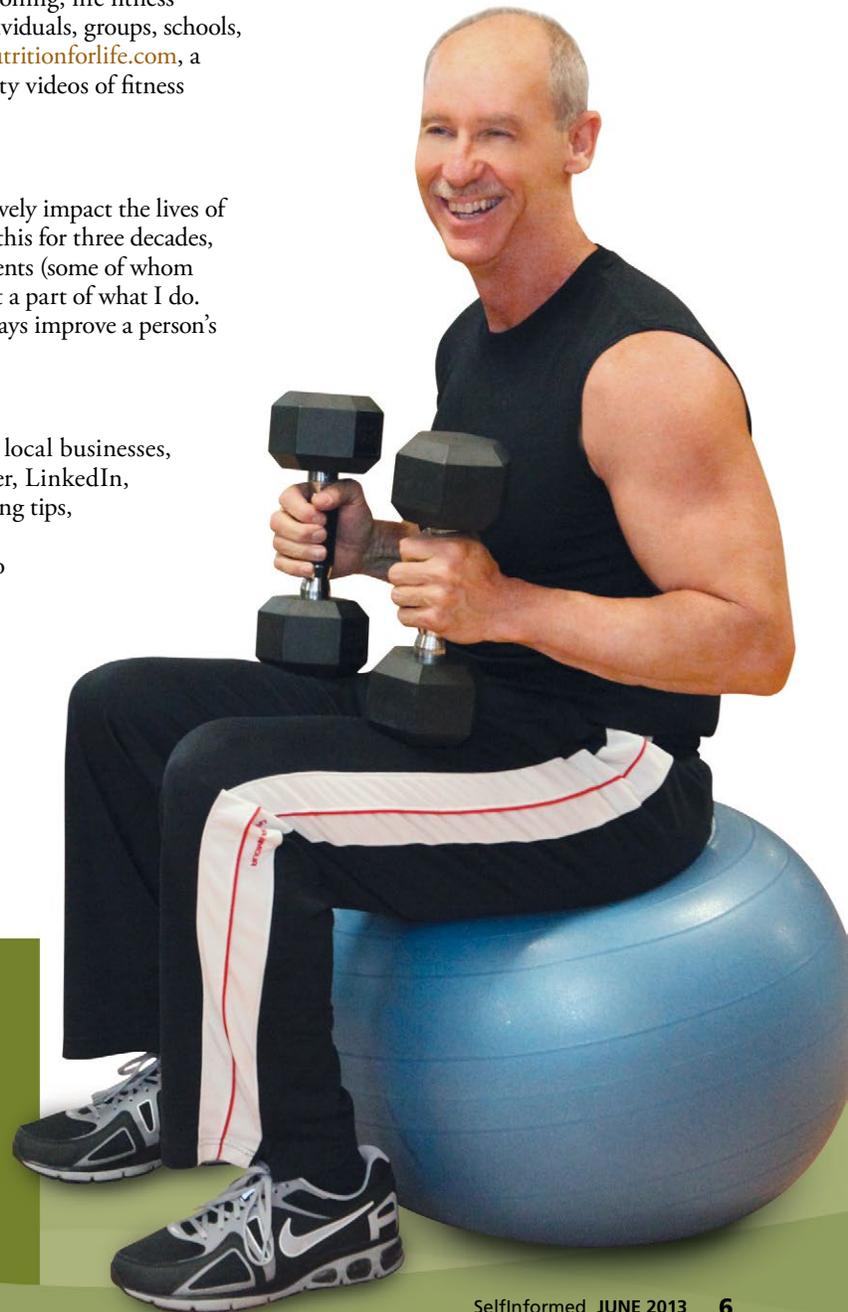
### How do you market your business?

I market my business through word of mouth referrals, other local businesses, handouts and flyers, and social media. I use Facebook, Twitter, LinkedIn, and Instagram. I try to provide pictures and videos when giving tips, advice, recipes, or motivational ideas because I believe pictures and videos bring articles to life and tell a better story. I'm also a musician and provide some of the backing tracks for the media, blending two of my passions together to help others.

### What advice would you offer to your fellow NASE Members?

I would advise my fellow members to utilize the many benefits for small businesses that they have access to through their membership. Everyone should take advantage of the advice available through Ask The Experts and learn from the many resources available on [NASE.org](http://NASE.org). ■

The discipline of proper training and a healthy lifestyle will always improve a person's emotional life and relationships with others and themselves.



## GET PUBLICITY FOR YOUR BUSINESS!

Your business could be featured in the *SelfInformed* Member Spotlight or another NASE publication. Let us know you'd like to be featured and tell us more about your business on our [Publicity Form](#).

## COLLECTION OF

# Online Sales Tax Looming



By Katie Vlietstra

Many business owners are following with interest the recent passage of the Marketplace Fairness Act of 2013 (S. 734) by the United States Senate. The legislation would allow for states to collect and remit sales taxes from Internet sales. Businesses with revenue less than \$1 million in online sales are exempt.

The bill does the following:

- implements minimum simplification requirements, including providing a single entity within the state responsible for all state and local sales and use tax administration, a single audit and tax return for all state and local jurisdictions, and a uniform sales and use tax base for all state and local taxing jurisdictions;
- adopts a uniform rule for sourcing all remote sales;
- provides information indicating the taxability of products and services and exemptions from tax;
- provides free software for remote sellers that calculates sales and use taxes, files tax returns, and updates tax rate changes;
- and provides remote sellers and certified software providers with a 90-day notice of tax rate changes.

The ability for states to collect sales tax from online sales would provide a much needed stream of revenue, and bring parity to businesses with a physical presence in those states. Supporters of the legislation argue that the existing disparity in sales tax collection harms brick-and-mortar businesses because they are required to charge and collect state and local taxes of between 5 and 10 percent.

Those against the legislation argue that the complexity of the regulatory burden placed on small businesses would be enormous. While the law requires free software for businesses to utilize, the sheer number of sales tax jurisdictions (9,600) would be challenging for any business, especially micro-businesses, to manage.

The NASE is currently reviewing the legislation and requesting feedback from our members to better inform our legislative strategy as it relates to Marketplace Fairness legislation. Make your voice heard by taking our [survey on the Marketplace Fairness Act](#). ■

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**Katie Vlietstra** is Director of Government Affairs of the NASE and provides critical insight to policymakers on issues affecting our nation's self-employed. You can contact her at [advocacy@NASE.org](mailto:advocacy@NASE.org).



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