

Small Business Tax Fundamentals and Raising Capital

Two critical concerns for any small business are understanding tax obligations and finding the money to grow. This course addresses both, covering the tax basics every small business owner needs to understand alongside the various options available for raising business capital. For CPAs and tax professionals, this is practical material that translates directly into better client conversations around cash flow planning, funding strategies, and keeping the business on solid financial footing.

CREDIT HOURS 2 | FIELD OF STUDY BUSINESS | EXAM QUESTIONS 10

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LEARNING ASSIGNMENTS AND OBJECTIVES

Assignment

- Study the full course materials included here.
- Complete the review questions after each chapter.
- Answer 10 final exam questions.
- Final exam is scored immediately, 70% or better passes.
- Certificate of completion is available in your account.
- Failed exams can be retaken free of charge.

Course Objectives

- Identify the deductible amounts of various small business expenses.
- Recognize the characteristics of various forms of crowdfunding.

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TABLE OF CONTENTS

CHAPTER

01

Tax Basics For The Small Business 4

1.01	Employer Identification Number	5
1.02	Form Ss-4, Application For Employer Identification Number	6
1.03	Becoming An S Corporation	9
1.04	Business Taxes In General	10
1.05	Business Deductions	18
1.06	Tax Audits	29
	Test Your Knowledge	34

CHAPTER

02

Raising Money For Your Business 38

2.01	Consider Writing A Business Plan	38
2.02	Two Types Of Outside Financing	43
2.03	Thirteen Common Sources Of Money	50
2.04	Document All Of The Money You Receive	57
2.05	Sample Promissory Note For Lump-Sum Repayment	57
	Test Your Knowledge	61

Final Exam Copy	73
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Glossary	65
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Index	
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Chapter 1: TAX BASICS FOR THE SMALL BUSINESS

Chapter Objective

After completing this chapter, you should be able to:

- Identify the deductible amounts of various small business expenses.

No matter whether your business is organized as a sole proprietorship, partnership, corporation, or limited liability company, you've automatically got a silent partner: Uncle Sam. The federal tax laws make this unavoidable. To guard against interest and penalties, you need to know what tax forms to file and when to file them. And to succeed in business, you need at least a basic, working knowledge of the tax system.

On a more positive note, by being aware of the fine points of the tax laws, you can often legally save a bundle of money—not to mention aggravation. For example, having a clear picture of what the IRS regards as a proper business expense will allow you to take deductions that otherwise might not occur to you.

Note: This chapter covers basic tax information that will already be familiar to most, however, it is helpful as a guide to ensure that all the basics are covered for the small business entrepreneur/start-up.

In addition to what you learn from books and other publications, you might have to hire a bookkeeper and an accountant. If you're operating a one-person small business out of your home, you might be able to keep your books and do your taxes with no professional help at all—or perhaps get help just the first time you file your annual tax return, to make sure you've correctly completed Schedules C (*Profit or Loss From Business*) and SE (*Self-Employment Tax*). On the other hand, if you've formed a corporation that's running a good-sized operation with eight employees, you might want an accountant to help set up your books and to prepare—or at least review—your business tax returns each year. And you might find that employing a part-time bookkeeper not only results in your records being well kept, but also frees you for more important tasks.

A word of caution about one other possible source of assistance: IRS employees. Most of them are hardworking and well-meaning, but their training and supervision are often inadequate. Unfortunately, it's common to receive poor oral advice in answer to questions. And if the advice proves to be so inaccurate that it results in your being assessed interest and penalties, the fact that you got it from an IRS employee won't get you off the hook. In short, it's often cheaper in the long

run to rely on the advice of an experienced small business accountant than on a free oral opinion from the IRS.

State taxes. In addition to federal taxes, you need to be aware of your state's tax scheme, which might include an income tax structured along the same lines as the federal version or one that has some major differences. Before you begin your business, contact your state's taxing authority to get detailed information. You'll also find helpful links at www.irs.gov/businesses/small-businesses-self-employed/state-government-websites.

EMPLOYER IDENTIFICATION NUMBER

You must get an Employer Identification Number (EIN) from the IRS when you start a business that you've set up as:

- A partnership
- An S corporation
- A C corporation
- A limited liability company (LLC) with two or more members, or
- A single-member LLC with employees or that you've chosen to have taxed as a corporation.

Technically, if you're a sole proprietor or the sole member of a limited liability company (LLC) that is not being taxed as a corporation and you have no employees, you can use your personal Social Security number instead of an EIN. But even in those situations, it's good business practice to get an EIN to differentiate cleanly between your personal and business finances.

You'll need your EIN before you file a tax return or make a tax deposit. In some cases, a bank will require you to have an EIN before you can open a business bank account.

How to Apply

To get an EIN, file Form SS-4, *Application for Employer Identification Number*.

The form isn't difficult to fill out if you follow the instructions. Nevertheless, these few pointers might help. (An example of Form SS-4 is included on the next page.)

Space 1. Insert your official corporate name if you're a corporation or your official company name if you're a limited liability company. If you're a partnership, use the partnership name shown in your partnership agreement. If you're a sole proprietor, insert your full name—the name you use on your personal tax return.

Space 12. Here you're asked to state the closing month of your business accounting year. Your answer, however, isn't binding. You make your binding election of a fiscal year-end on the first federal income tax return that you file for the business.

FORM SS-4, APPLICATION FOR EMPLOYER IDENTIFICATION NUMBER

Form SS-4 (Rev. December 2023) Department of the Treasury Internal Revenue Service	Application for Employer Identification Number (For use by employers, corporations, partnerships, trusts, estates, churches, government agencies, Indian tribal entities, certain individuals, and others.) See separate instructions for each line. Keep a copy for your records. Go to www.irs.gov/FormSS4 for instructions and the latest information.	OMB No. 1545-0003 EIN _____
Type or print clearly.	1 Legal name of entity (or individual) for whom the EIN is being requested _____	
	2 Trade name of business (if different from name on line 1) _____	3 Executor, administrator, trustee, "care of" name _____
	4a Mailing address (room, apt., suite no. and street, or P.O. box) _____	5a Street address (if different) (Don't enter a P.O. box.) _____
	4b City, state, and ZIP code (if foreign, see instructions) _____	5b City, state, and ZIP code (if foreign, see instructions) _____
	6 County and state where principal business is located _____	
	7a Name of responsible party _____	7b SSN, ITIN, or EIN _____
	8a Is this application for a limited liability company (LLC) (or a foreign equivalent)? ☐ Yes ☐ No	
	8b If 8a is "Yes," enter the number of LLC members _____	
	8c If 8a is "Yes," was the LLC organized in the United States? ☐ Yes ☐ No	
	9a Type of entity (check only one box). Caution: If 8a is "Yes," see the instructions for the correct box to check. <div style="display: flex; justify-content: space-between;"> <div style="width: 48%;"> ☐ Sole proprietor (SSN) _____ ☐ Partnership _____ ☐ Corporation (enter form number to be filed) _____ ☐ Personal service corporation _____ ☐ Church or church-controlled organization _____ ☐ Other nonprofit organization (specify) _____ ☐ Other (specify) _____ </div> <div style="width: 48%;"> ☐ Estate (SSN of decedent) _____ ☐ Plan administrator (TIN) _____ ☐ Trust (TIN of grantor) _____ ☐ Military/National Guard ☐ State/local government ☐ Farmers' cooperative ☐ Federal government ☐ REMIC ☐ Indian tribal governments/enterprises Group Exemption Number (GEN) if any _____ </div> </div>	
9b If a corporation, name the state or foreign country (if applicable) where incorporated <div style="display: flex; justify-content: space-between;"> <div style="width: 40%;">State _____</div> <div style="width: 60%;">Foreign country _____</div> </div>		
10 Reason for applying (check only one box) ☐ Started new business (specify type) _____ ☐ Banking purpose (specify purpose) _____ ☐ Changed type of organization (specify new type) _____ ☐ Purchased going business _____ ☐ Hired employees (Check the box and see line 13.) _____ ☐ Created a trust (specify type) _____ ☐ Compliance with IRS withholding regulations _____ ☐ Created a pension plan (specify type) _____ ☐ Other (specify) _____		
11 Date business started or acquired (month, day, year). See instructions. _____		
12 Closing month of accounting year _____		
13 Highest number of employees expected in the next 12 months (enter -0- if none). If no employees expected, skip line 14. <div style="display: flex; justify-content: space-around; margin-top: 10px;"> Agricultural _____ Household _____ Other _____ </div>		
14 If you expect your employment tax liability to be \$1,000 or less in a full calendar year and want to file Form 944 annually instead of Forms 941 quarterly, check here. (Your employment tax liability will generally be \$1,000 or less if you expect to pay \$5,000 or less, \$6,536 or less if you're in a U.S. territory, in total wages.) If you don't check this box, you must file Form 941 for every quarter. ☐		
15 First date wages or annuities were paid (month, day, year). Note: If applicant is a withholding agent, enter date income will first be paid to nonresident alien (month, day, year) _____		
16 Check one box that best describes the principal activity of your business. <div style="display: flex; justify-content: space-between;"> <div style="width: 48%;"> ☐ Construction ☐ Rental & leasing ☐ Transportation & warehousing ☐ Real estate ☐ Manufacturing ☐ Finance & insurance ☐ Other (specify) _____ </div> <div style="width: 48%;"> ☐ Health care & social assistance ☐ Wholesale—agent/broker ☐ Accommodation & food service ☐ Wholesale—other ☐ Retail </div> </div>		
17 Indicate principal line of merchandise sold, specific construction work done, products produced, or services provided. _____		
18 Has the applicant entity shown on line 1 ever applied for and received an EIN? ☐ Yes ☐ No If "Yes," write previous EIN here _____		
Third Party Designee	Complete this section only if you want to authorize the named individual to receive the entity's EIN and answer questions about the completion of this form.	
	Designee's name _____ Address and ZIP code _____	Designee's telephone number (include area code) _____ Designee's fax number (include area code) _____

Sole proprietors, partnerships, S corporations, personal service corporations, and limited liability companies are generally required to use a calendar year—that is, a year ending December 31—for tax purposes. Personal service corporations have two basic characteristics:

- The professional employees of the corporation own the stock, and
- The corporation performs its services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting.

To use a tax year other than a calendar year, an S corporation must demonstrate to the IRS that there is a substantial business reason to do so, such as the seasonal nature of the business. Basically, the IRS wants to make sure that permitting you to claim a tax year other than the calendar year won't substantially distort your income.

Resource

For details about choosing your tax year, see “Business Purpose Tax Year,” in IRS Publication 538, *Accounting Periods and Methods*.

A C corporation that's not a personal service corporation is freer to choose a fiscal year. Most small businesses find that where there's a choice, the calendar year is the most convenient way to proceed. Sometimes, however, there are tax planning reasons for a business owner to choose a different tax year for the business.

Example 1

Radcraft, Inc., a C corporation, selects the calendar year for its fiscal year. In December 2025, it pays a \$30,000 bonus to Jill, the president and sole shareholder. The bonus is included on Jill's 2025 income tax return, and tax on the bonus is due in April 2026.

Example 2

Jill selects a fiscal year of February 1 through January 31 for Radcraft, Inc. (On Form SS-4, she lists January in space 12 for the closing month of the corporation's accounting year.) In January 2025, the corporation pays Jill a \$30,000 bonus. The bonus is included in Jill's 2025 income tax return. This means that the tax on the bonus isn't due until April 2026—although Jill must keep track of it when computing her quarterly estimates in 2025.

Space 13. These numbers can be estimated. It's usually best to estimate on the low side.

Space 15. The IRS will send you computer-generated payroll tax forms based on your answer to this question.

Space 18. This question refers to the business, not the owner. Normally, a partnership, corporation, or limited liability company has only one EIN. A sole proprietor might have several businesses, each with a separate number.

After filling out the form, there are three ways to obtain the number:

- **Online.** The simplest and fastest way to get an EIN is to complete Form SS-4 online at www.irs.gov. You'll receive your EIN instantly.
- **By fax.** You can fax your Form SS-4 to 855-641-6935.
- **By mail.** If you have enough lead time, you can mail Form SS-4 to the IRS and wait for the number to be mailed to you, which will take four to five weeks. Mail your completed Form SS-4 to Internal Revenue Service, Attn: EIN Operation, Cincinnati, OH 45999.

Use your EIN on all business tax returns, checks, and other documents you send to the IRS. Your state taxing authority might also require your EIN on state tax forms.

When to Get a New Number

If your S corporation chooses to change to a C corporation—or your C corporation chooses to change to an S corporation—it doesn't need a new EIN; the one you already have is still sufficient. However, you'll need to get a new EIN if any of these changes occur in your business:

- You incorporate your sole proprietorship or partnership.
- You convert your sole proprietorship or partnership to a limited liability company.
- Your sole proprietorship takes in partners and begins operating as a partnership.
- Your partnership is taken over by one of the partners and begins operating as a sole proprietorship.
- Your corporation changes to a partnership or to a sole proprietorship.
- You purchase or inherit an existing business that you'll operate as a sole proprietorship.
- You represent an estate that operates a business after the owner's death.
- You terminate an old partnership and begin a new one.

Filing Form SS-4 for an LLC

A multi-member LLC, which the IRS treats as a partnership unless you elect corporate tax treatment, must obtain an EIN whether or not it will have employees.

As previously discussed, a single-member LLC is treated as a sole proprietorship for tax purposes, unless you elect corporate tax treatment. You can use your Social Security Number (SSN) as the EIN of the business if you won't have employees. You must obtain an EIN for your single-member LLC if you'll have employees. You can choose to obtain a separate EIN for the business for banking or other reasons. You would use the separate EIN on Schedule C of your Form 1040.

If you're electing corporate tax treatment (probably S corporation status) for your LLC, you would check the "Corporation" box on Line 9a of Form SS-4.

BECOMING AN S CORPORATION

Many corporations derive tax benefits from choosing S corporation status. The difference between a C corporation, which is a separate tax entity from its shareholders, and an S corporation, whose income is reported on the owners' tax returns, is described in some detail in Chapter 1 of course 82601A. If you're not thoroughly familiar with this material, please reread it before going on.

To become an S corporation, all shareholders must sign and file IRS Form 2553, *Election by a Small Business Corporation*, with the IRS by the 15th day of the third month of the tax year to which the election is to apply.

Example

Mia, James, and Evelyn form a corporation, Phoenix Ventures, Inc. They start to do business on September 1, 2025 and, like most businesses, use the calendar year for accounting and tax purposes. Their 2025 tax year will be a short one: September 1 through December 31. To obtain S corporation status for 2025, they must file Form 2553 by November 15, 2025, which is the 15th day of the third month of that tax year. If they miss that deadline, their corporation won't qualify for S corporation status in 2025. But if they file Form 2553 by March 15, 2026, their corporation will get S corporation status for 2026.

A number of technical rules govern which corporations can elect to become S corporations. Your corporation must meet these requirements:

- It must be a domestic corporation—one that's organized under U.S. federal or state law.
- It must have only one class of stock.

- It must have no more than 100 shareholders.
- It must have as shareholders only individuals, estates, and certain trusts. Partnerships and corporations can't be shareholders in an S corporation.
- It can't have any shareholder who is a nonresident alien.

There are other technical rules, but the vast majority of new, small corporations may become S corporations if they choose to do so.

To elect S corporation status, you need the consent of all shareholders. Unless yours is a one-person corporation, you should agree on this election before you form your corporation.

An S corporation election doesn't have to be permanent. You can start out as an S corporation and then, after a few years, revoke your S corporation status and be taxed as a C corporation. If you terminate your status as an S corporation, generally you'll have to wait five years until you can again become an S corporation—although you might be able to get permission from the IRS to shorten this waiting period.

Once the shareholders file Form 2553, the corporation continues to be an S corporation each year until the shareholders revoke that status or it's terminated under IRS rules. What terminates S corporation status? For one thing, ceasing to qualify as an S corporation. For example, your corporation would no longer qualify if it had more than 100 shareholders or if you or another shareholder transferred some of your stock to a partnership.

BUSINESS TAXES IN GENERAL

Three main categories of federal business taxes might apply to your business:

- Income tax
- Employment tax, and
- Self-employment tax.

This section looks briefly at each of these tax categories. Get IRS Publication 509, *Tax Calendars*, to see when to file returns and make tax payments. It's updated annually.

Excise taxes. In addition to the three main business taxes, the federal government imposes excise taxes on a few specialized transactions and products. These taxes almost never are of concern to small businesses. To see whether your business is affected, see IRS Publication 334, *Tax Guide for Small Business*.

Income Tax

You must file an annual federal tax return reporting your business income. Following is a list of the forms to use.