

# 1065 Sample Return

Frank Able and Susan Baker, partners of AbleBaker Bookstore, have just come into your office to have their partnership tax return prepared. Let's quickly prepare a partnership tax return for the AbleBaker Bookstore and learn about some of the features in the program.

## Step 1 – Start-Up

- A** Double click the **Program icon** on your desktop.
- B** The program should automatically open to the *Client Selection* screen. If not, click the **Clients** button on the button bar.

## Step 2 – Folder Selection

- A** Click the **1065** tab.
- B** Create a new folder by clicking **Edit** on the menu bar and selecting **New Folder** from the list.
- C** Type **Tutorial** in the *New Folder Name* field and click **OK**.

## Step 3 – Client Selection

- A** A database will maintain a list of clients already in your folder. Since the AbleBaker Bookstore partnership is new, click the **New Client** button.

## Step 4 – New Client

- A** The *New Client* screen will appear, enabling you to initialize the client.
- B** To move from field to field, use your mouse or press the **Enter**, **Tab**, or **Arrow** keys. Press the **Shift** and **Tab** keys together to move back a field.
- C** Enter the *Client Number* as **1**.
- D** Enter the *Client ID* as **ABLE9999** (we have used the first four letters in the partnership name and the last four digits of the EIN).

### Note

The *Client ID* and *Client No.* fields are optional entries. They may be left blank or any combination of letters and/or numbers may be used.

- E** Enter the *Partnership Name* as **AbleBaker Bookstore**. An input field for the second name, if applicable, is provided.
- F** Enter the *EIN* without a dash, as it is already provided. AbleBaker Bookstore's EIN is **10-9999999**.

**G** Enter the address as **334 North Main Street**.

**1** AbleBaker Bookstore's zip code is **20904**.

## Note

There are no fields for the city and state. Simply enter the zip code and the program will insert the city and state on the *General Information* screen. If the zip code represents more than one city, the program will open a window with a selection of cities for that zip code. Select the correct city by highlighting it.

**2** AbleBaker Bookstore's city is **Silver Spring**.

**H** Click **OK** to continue.

### Step 5 – General Information

**A** The first input screen will appear. This is the *General Information* screen. Notice that the Client ID, partnership's name, address, city, state, zip, county, and EIN have all carried from the *New Client* screen.

**B** The partnership is a calendar year partnership. The *Fiscal/Short Year* is not applicable for this return. Leave this area blank.

**C** The business activity for AbleBaker Bookstore is **Retail**. Highlight the *Business Activity* input field. Click the down arrow (▼) button on the drop down box. A listing of the principal business activities will appear in a tree format based on the North American Industry Classification System in the IRS form instructions. Find *Retail Trade* and click the **plus (+) sign** to expand the tree. A more detailed listing will appear. Select **Book Stores**. The program will insert the *Principal Business Activity* as **Retail Trade**, the *Principal Product or service* as **Book Stores** and the *Business Code Number* as **451211**.

**D** Enter the date the business started as **10-01-80**.

**E** The *Method of Accounting* is **Accrual**.

**F** For this tutorial, enter your firm's email address on the Email address line.

### Step 6 – Preparer Options

We will now go to the *Preparer Options* screen indicated in the Forms pane as **PO - Options**. Frank and Susan want to produce financial statements in the program in order to determine their ability to obtain financing for a future real estate investment. The financial statements prepared on a tax basis include a *Statement of Revenue and Expenses*, a *Balance Sheet*, and a *Statement of the Partner's Capital*.

**A** Check the box to **Prepare financial statements**.

Frank and Susan also want the *Two-Year Comparison Worksheet*. This worksheet lists the ordinary income, expenses, and Schedule K amounts for the current and prior years and computes the differences between them.

**B** Check the box to **Prepare two-year comparison worksheet**.

### **Step 7 – 1065, page 1, Ordinary Income and Expenses**

Let's start by entering the ordinary income and expenses on page 1 of Form 1065 for the AbleBaker Bookstore.

**A** In the Forms pane, click on **1 - 1065 Pg 1**.

**B** Enter the following ordinary income in the appropriate field in the Input pane:

Gross receipts or sales, line 1a . . . . . **\$409,465**

Returns and allowances, line 1b . . . . . **\$3,365**

Interest income on accounts receivable, line 7\* **\$559**

\* We will create a detail statement on line 7 for the interest income of \$559. Put the cursor on the line 7 input field, then click the **Detail** button on the button bar. Enter the description as **Interest income on accounts receivable**. Enter the amount as **\$559**.

**C** Click **OK** to return to the 1065, page 1 input screen.



When you move from this field, the color of the field will change, indicating that it was detailed. The total amount will also appear.

**D** Enter the following allowable deductions in the appropriate input fields:

|  |                 |
|--|-----------------|
| Salaries and wages, line 9 . . . . .                 | <b>\$29,350</b> |
| Guaranteed payments to partners, line 10 . . .       | <b>\$25,000</b> |
| (Frank received \$20,000 and Susan received \$5,000) |                 |
| Repairs and maintenance, line 11 . . . . .           | <b>\$1,125</b>  |
| Bad debts, line 12 . . . . .                         | <b>\$250</b>    |
| Real Property, line 13 . . . . .                     | <b>\$20,000</b> |
| State Income Taxes, line 14 . . . . .                | <b>\$3,295</b>  |
| Interest, line 15 . . . . .                          | <b>\$1,451</b>  |
| Other Deductions, line 20                            |                 |
| Advertising . . . . .                                | <b>\$4,000</b>  |
| Other business deductions* . . . . .                 | <b>\$4,003</b>  |

\* We will create a detail statement for the other business deductions of \$4,003. Put the cursor on the line 20 input field for *Other business deductions*, then click the **Detail** button. Enter the descriptions as **Labeling Costs** and **Miscellaneous Deductions** on separate lines. Enter the amounts as **\$3,000** and **\$1,003**, respectively.

**E** Click **OK** to return to the 1065, page 1 input screen.

**F** On the button bar, click the **Peek** button to view the output form. Check to make sure the *Total Other Deductions* of **\$8,003** is printing on line 20.

## **Step 8 – Depreciation**

The partnership has bookshelves that they are currently depreciating. The bookshelves were purchased in one transaction. Therefore, they will be set up as one asset. We will use the *Asset Tracker* to help track the depreciation.

**A** Click the **Assets** button located on the button bar to open the *Asset Tracker*.

- B** Click the **New** button to add the asset.
  - 1** Make sure the *Form* is set to **1065**.
  - 2** Enter the *Description* as **Shelves**.
  - 3** The shelves were purchased on **05-01-2010**.
  - 4** The *Type* is **Furniture and Fixtures**.
  - 5** The *Prior Depreciation* is **\$480**.
  - 6** The *Cost* was **\$3,356**.
  - 7** The *Method* should default to **MACRS 7 Year (M7YR)**.
  - 8** Click **OK** to continue. You are now on the General tab of the *Asset Tracker*.



Select the *Type* by clicking ▼ in the *Type* field, or start typing **Furniture** to use the auto-fill feature. This is an optional entry.

- 9** The *Current Depreciation* should be **\$822**.
  - 10** Enter **\$480** as the *Prior Depreciation* in the *AMT* column.
- C** Click **Close** to exit the *Asset Tracker* and return to the 1065, page 1 input screen.

### Step 9 – 1125A, Cost of Goods Sold

- A** From the *Forms Selection* pane, click on **Form 1125-A, Cost of Good Sold**.

- 1** Enter the following amounts:

|  |                  |
|--|------------------|
| Inventory at beginning of year, line 1 . . . . . | <b>\$18,125</b>  |
| Purchases, line 2 . . . . .                      | <b>\$268,741</b> |
| Inventory at end of year, line 7 . . . . .       | <b>\$19,225</b>  |

- 2** Line 8, *Cost of goods sold*, will automatically calculate and should equal \$267,641.
- 3** The *method* used for valuing inventory for the partnership is **Cost**, which is the default method in the program. Therefore, no entry is necessary.
- 4** The remaining questions regarding inventory are answered No by default for the partnership. You do not need to make any entry.

- B** Again from the forms selection pane, select the *Form 1065, page 1* input screen.
- C** Click the **Peek** button on the button bar to review the numbers on the form. As a result of the *Cost of goods sold* entries, Form 1065, page 1 should show the following:

Total income, line 8. . . . . \$139,018  
 Total deductions, line 21 . . . . . \$89,296  
 Ordinary business income, line 22 . . . . . \$49,722

### **Step 10 – 1065, page 2 & 3, Other Information, Schedule B**

The AbleBaker Bookstore is a Domestic General Partnership, which is the default in the program. Therefore, an entry on line 1 of Schedule B is not necessary. In addition, the partners will all be treated as general partners on the Schedule K-1s.



The questions on lines 2 and 4-16 are answered No by default for the partnership. Question 3 will automatically be produced based on information entered on the Partner K-1s, to be entered later in this tutorial. Also, question 17, the last question on Schedule B deals with foreign partnerships and is not applicable for this return.

### **Step 11 – 1065, page 4, Schedule K**

- A** In the Forms pane, click on **4 - 1065 pg 4**.
- B** The partnership has several items that must be reported separately on Schedule K.
  - 1** Click the *Interest* grid button on line 5. Enter the *Interest Income Description of Maryland Municipal Bonds*. In the *Total Muni Bonds* column, enter **50**. Note that the resident state of **MD** appeared in the *State* column. This state can be changed to indicate the state that issued the bonds, if needed. The tax-exempt interest will carry to line 18a of Schedule K. Click the **Close** button.
  - 2** Click the **Dividends** grid button on line 6. Enter the *Dividend Income Description of Amazon.com Stock*. Press the **Tab** key to move to column 1a and enter **150** as the *Total Ordinary Dividends*. Press the **Tab** key to move to column 1b. Notice that the **150** automatically appears in column 1b. This is to help eliminate key strokes, as most ordinary dividends are also qualified dividends. Column 1b can be changed if necessary. Click **Close** to return to the 1065, page 4 input screen.

- 3** We will create a *Detail Statement* for the contributions for line 13. Click the line 13a, *Cash contributions (50%)*, input field, then click the **Detail** button on the button bar and select **Detail Statement**. Enter the descriptions as **United Way** and **American Cancer Society** on separate lines. Enter the amounts as **300** and **350**, respectively. Close the grid. Click **Peek** to view the full form. Verify that line 13a shows the total contributions of \$650.
- C** Enter **\$52,880** on line 19a, *Distributions of cash and marketable securities*. Frank and Susan each withdrew \$26,440 from the partnership.

## **Step 12 – 1065, page 5, Analysis of Net Income**

- A** In the Forms pane, click on **5 - 1065 pg 5**.

### **Note**

The *Analysis of Net Income* section will be automatically filled out based on the type of partners indicated on the Schedule K-1 input screen. The Schedule K-1 input will be deferred to a later step in this tutorial.

## Step 13 – 1065, page 5, Balance Sheet

- A** Enter the AbleBaker Bookstore beginning and ending balance sheet amounts as shown below:

|  | Beginning of<br>Tax Year | End of<br>Tax Year |
|--|--------------------------|--------------------|
| Cash, line 1   | <b>\$9,981</b>           | <b>\$9,181</b>     |
| Notes and accounts<br>receivable, line 2a                  | <b>\$7,150</b>           | <b>\$10,990</b>    |
| Tax-exempt securities, line 5*<br>Maryland Municipal Bonds | <b>\$1,000</b>           | <b>\$1,000</b>     |
| Bldg/other depreciable<br>assets, line 9a                  | <b>\$3,356</b>           |                    |
| Accumulated depreciation,<br>line 9b                       | <b>\$320</b>             |                    |
| Accounts payable, line 15                                  | <b>\$8,742</b>           | <b>\$8,329</b>     |
| Mortgages, notes, bonds<br>under 1 yr, line 16             | <b>\$3,000</b>           | <b>\$2,600</b>     |
| Mortgages, notes, bonds<br>over 1 yr, line 19              |                          | <b>\$7,739</b>     |

\* For the *Tax-exempt securities*, line 5, create a Detail Statement by clicking the **Detail** button on the button bar and using *Maryland Municipal Bonds* as the description. Notice that the detail statements on the balance sheet allow the beginning and ending amounts for the year to be entered.

- B** Scroll down below the balance sheet to locate Schedule M-2, *Analysis of Partners' Capital Accounts*. Enter **\$27,550** as the balance at the beginning of the year on line 1 of Schedule M-2. The M-2 beginning and ending balances for the year will automatically carry to the balance sheet, line 21.

- C** Verify the following amounts by clicking the **Peek** button on the button bar to view the form. These amounts should automatically carry and print on the balance sheet of Form 1065, page 5:

|   | Beginning of<br>Tax Year | End of<br>Tax Year |
|---|--------------------------|--------------------|
| Inventories, line 3*                        | <b>\$18,125</b>          | <b>\$19,225</b>    |
| Bldg/other depreciable<br>assets, line 9a ^ |                          | <b>\$3,356</b>     |
| Accumulated depreciation,<br>line 9b ^      |                          | <b>\$656</b>       |
| Total assets, line 14                       | <b>\$39,292</b>          | <b>\$43,096</b>    |
| Partners' capital account,<br>line 21 ~     | <b>\$27,550</b>          | <b>\$24,285</b>    |
| Total Liabilities and Capital,<br>line 22   | <b>\$39,292</b>          | <b>\$43,096</b>    |

\* This field carries automatically from Schedule A, *Cost of Goods Sold*.

^ This field carries automatically from the *Asset Tracker*.

~ This field carries automatically from Schedule M-2.

## Note

In the subsequent year, the beginning balance sheet amounts need not be entered because the amounts will carry from the prior year ending balance sheet amounts to the subsequent year beginning balance sheet amounts during the Update process. The detail statements will also be updated.

### Step 14 – 1065, page 5, Schedule M-1

No entries are required for the AbleBaker Bookstore because all of the M-1 items carry automatically from other parts of the return.

- A** Scroll down to the bottom of the input screen to locate Schedule M-1, *Reconciliation of Income per Books with Income per Return*.
- B** Click **Peek** to view the output screen.
- C** On line 3, *Guaranteed payments* of \$25,000 automatically carried from page 1, line 10.
- D** On line 6, *Tax exempt interest* of \$50 automatically carried from page 4, Schedule K, line 18a.
- E** On line 7a, *Depreciation* of \$486 automatically carried from the *Asset Tracker*.
- F** On line 9, *Income (loss)* of \$74,222 automatically carried from page 5, Analysis of Net Income (Loss), line 1.

**G** On line 1, *Net income (loss) per books* of \$49,758 was computed based on the above amounts.

**H** Click **Peek** to return to the input screen.

### **Step 15 – 1065, page 5, Schedule M-2**

**A** Scroll below Schedule M-1 to locate Schedule M-2.

**B** The \$27,550 for the balance at the beginning of the year for the Partners' Capital Accounts was entered in Step 13. This amount will carry to Schedule L. In the subsequent year, it is not necessary to enter this amount because it will be updated and reflect the prior year's ending balance amount.

**C** Click **Peek** to view the output form.

**D** On line 3, *Net income (loss) per books* of \$49,758 carried automatically from Schedule M-1, line 1.

**E** On line 6, *Distributions* of \$52,880 carried automatically from Schedule K, line 19a.

**F** On line 9, *Balance at end of year* of \$24,428 was computed based on the above amounts.

**G** Click **Federal** to return to the input screen.

### **Step 16 – Schedule K-1, Frank W. Able**

We need to enter Frank's K-1 information.

**A** In the Forms pane, click on **K1 - Partner K-1**.

**B** Notice the *Prior*, *Next*, and *1 of 1* buttons at the top of the input screen. This screen is set up as a multiple input screen where up to 10,000 K-1s may be entered.

**C** Enter **Frank W. Able** as the *Partner's name* (top line).

**D** Enter Frank's *Street Address* as **10 Green Street**.

**E** Enter the *ZIP code* as **20904**.

**F** Select **Silver Spring** as the city.

**G** Enter Frank's *SSN* as **123-00-6789**.

**H** Check the box to indicate that Frank is the *Tax Matters Partner*. The required information will carry automatically to page 2 of the 1065.

**I** If you **peek** the form, you will notice for item G that the box for *General partner* is automatically checked on the form because this is a General Partnership.

- J** Click **Peek** to return to the input screen.
- K** Select **7, Individual – Active** from the drop down box for the *Type of entity* field on item I.
- L** Enter **50%** in the *Master Default %* field for item J since Frank’s percentage of profit sharing, loss sharing, and ownership of capital is 50%.
- M** Enter **\$14,050** for Frank’s *Beginning Capital* for item L, *Partner’s capital account analysis*. The remaining amounts from item L are automatically computed. In the subsequent year, you need not enter the beginning capital account because the ending capital account for the prior year will update to the beginning capital account for the subsequent year.
- N** Enter **\$20,000** on line 4, *Guaranteed Payments to Partner*, of part III for Frank’s guaranteed payment. Frank’s guaranteed payment and his share of ordinary income will be subject to Self-Employment Tax. The program will carry the self-employment earnings to line 14a.
- O** All remaining amounts will carry automatically to Schedule K-1 from Schedule K.

### **Step 17 – Schedule K-1, Susan L. Baker**

Now we need to enter Susan’s K-1 information.

- A** At the top of Frank’s K-1 input screen, click the **Next** button to access the second K-1.
- B** Notice that at the top of the input screen, next to the *Prior* and *Next* buttons, we see *2 of 2*.
- C** Enter **Susan L. Baker** as the *Partner’s name* (top line).
- D** Enter Susan’s *Street Address* as **10 Orange Street**.
- E** Enter the *ZIP code* as **20904**.
- F** Select **Silver Spring** as the city.
- G** Enter Susan’s *SSN* as **546-01-3333**.
- H** If you **peek** the form, you will notice for item G, that the box for *General partner* is automatically checked on the form because this is a General Partnership.
- I** Click **Peek** to return to the input screen.
- J** Select **7, Individual – Active** from the drop down box for the *Type of entity* field on item I.

- K** Enter **50%** in the *Master Default %* field for item J since Susan's percentage of profit sharing, loss sharing, and ownership of capital is 50%.
- L** Enter **\$13,500** for Susan's *Beginning Capital* for item L, *Partner's capital account analysis*. The remaining amounts from item L are automatically computed. In the subsequent year, you need not enter the beginning capital account because the ending capital account for the prior year will update to the beginning capital account for the subsequent year.
- M** Enter **\$5,000** on line 4, *Guaranteed Payments to Partner*, of part III for Susan's guaranteed payment. Susan's guaranteed payment and her share of ordinary income will be subject to Self-Employment Tax. The program will carry the self-employment earnings to line 14a.
- N** All remaining amounts will carry automatically to Schedule K-1 from Schedule K.

### **Step 18 – Self-Employment Worksheet**

Because Frank and Susan are general partners and their income is subject to Self-Employment Tax, the total net earnings of \$74,722 will carry to Schedule K, line 14a. In addition, the *Self-Employment Worksheet* will be produced. The worksheet is a duplicate of the worksheet found in the IRS form instructions. To view the worksheet, the return must be reviewed (Step 21).

## Step 19 – Two-Year Comparison

Frank and Susan want a Two-Year Comparison report so they can identify any significant changes in amounts reported in 2011 versus the amounts reported in 2010. In Step 6, Preparer Options, the *Two-Year Comparison* box was checked. However, because this is a new client, the 2010 amounts must be manually input. In subsequent years, the report will be updated for the prior year amounts.

**A** In the Forms pane, click **2YR-2Yr Comp P1**.

**B** Enter the following amounts for the prior year:

Income:

|                                       |                  |
|---------------------------------------|------------------|
| Gross receipts or sales . . . . .     | <b>\$300,000</b> |
| Less returns and allowances . . . . . | <b>\$3,000</b>   |
| Cost of goods sold . . . . .          | <b>\$250,000</b> |
| Other income . . . . .                | <b>\$50</b>      |

Deductions:

|   |                 |
|---|-----------------|
| Salaries and wages . . . . .              | <b>\$25,000</b> |
| Guaranteed payments to partners . . . . . | <b>\$25,000</b> |
| Repairs and maintenance . . . . .         | <b>\$2,000</b>  |
| Bad debts . . . . .                       | <b>\$200</b>    |
| Rent . . . . .                            | <b>\$20,000</b> |
| Taxes and licenses . . . . .              | <b>\$2,500</b>  |
| Interest . . . . .                        | <b>\$1,400</b>  |
| Depreciation . . . . .                    | <b>\$320</b>    |
| Other deductions . . . . .                | <b>\$5,000</b>  |

Schedule K:

|   |                 |
|---|-----------------|
| Guaranteed payments to partners . . . . . | <b>\$25,000</b> |
|---|-----------------|

**C** In the Forms Pane, click **2YR2-2Yr Comp P2**.

**D** Enter the following amount for the prior year:

Self-Employment:

Net earnings from self-employment . . . . . **\$32,320**

## **Step 20 – State Instructions**

The AbleBaker Bookstore also operates a store in Washington, D.C. The partnership is required to file a Washington, D.C. Partnership Return of Income.

**A** Click the **State** button on the button bar. It should have the Maryland State flag on it since Maryland was entered as the incorporation state on the *Federal General Information* input screen.

**B** Click the **States...** button.

**C** Notice that Maryland is already entered as the resident (organization or incorporation) state.

**D** Select **DC** from the drop down box as the *2nd state*. Then click the **Close** button.

**E** Click the ▼ on the *State* drop down box located on the Forms Pane. Select **DC** from the list of states.

**F** The state information will carry directly from the federal inputs. If you would like to override any values, you may do so now.

## **Step 21 – Review the Return**

Now let's review the return. The program will produce Form 1065, pages 1 through 5; Schedules K-1 for Frank and Susan; a Two-Year Comparison; Financial Statements; Form 4562; and a Detail Statement. The program will also produce a Self-Employment Worksheet, a Federal Depreciation Schedule, a Partner's Summary, Schedule M-1 explanation, Partner's current year increase/decrease worksheet, an instruction letter for the Partnership, a K-1 letter with each K-1, an invoice, and state forms.

**A** Click the **Review** button on the button bar.

**B** The program produces some audit statements that may provide useful information or help identify trouble spots in the return. This return should produce only one green FYI audit. However, if you do see some audits while processing client tax returns, they should be resolved before filing the returns, if possible; green audits, which are reminders and FYI information audits, require no further action.

## Step 22 – Compare 1065, Pages 1-5, Schedules K-1

In the *Samples* directory, you will find a copy of the AbleBaker Bookstore return. Review the return, print out Form 1065, pages 1 through 5, and Schedules K-1. Compare them to the return that you have entered in the *Tutorial* folder.

## Step 23 – Printing the Return

You have various options for printing.

- A** You can print or save the return.
- B** There are several ways to print *all* of the forms:
  - 1** Click the ▼ in the *Print* drop down box and select **All**. Then click the **Print** button.
  - 2** Select all of the forms by clicking the checkbox at the very top of the Output Forms list. Select **Tagged** from the *Print* drop down box and then click the **Print** button.
- C** To print specific forms, tag the forms you want to print by checking the box next to the form in the Output Forms list. Select **Tagged** from the *Print* drop down box and then click the **Print** button.
- D** To print only one specific form, highlight the form, make sure **Page** is selected in the *Print* drop down box, and click the **Print** button.
- E** To save the return in PDF file, tag the forms you want to save and click the **Adv.** button. In the *Save* section of this screen, select **Tagged** from the *Set* drop down box. Click the **Browse (...)** button to find the appropriate location. Click the **Start Job** button.

## Step 24 – Exiting the Return

When you are finished printing or viewing the return, use the following steps to exit.

- A** Click the **Clients** button on the button bar. This will take you back to the *Client Selection* screen.
- B** Or, you may click the **Close** button on the button bar. This will close the client. You can then exit the program by selecting **Exit** from the *File* menu.

### Note

Saving a return will save the PDF file in a location that you specify on your computer. If you have installed the ArkWorks program, you can automatically archive tax returns to ArkWorks by clicking the **ArkWorks** button.

## Congratulations!

You have just completed the 1065 Sample Return.