10 REASONS TO STOP & THINK ABOUT TAXES

What every business owner should be doing with their tax position now.

RecordsInOrder

Tax Strategy for Small Business Owners
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INTRODUCTION

It is usually not just one thing.

It is several details that you pay attention to and bring together to increase business success. And so, it is with tax savings. You generally don't implement one big thing, and certainly not an "edge of the cliff" tax position. It's the detail of advanced planning that makes up effective tax strategy for your best tax position, and the resulting tax savings.

You're busy, just about all the time, but just stop for a minute and take an assessment of some of the things you might NOT be doing that would improve your tax status.

HERE ARE YOUR 10 REASONS:

1) No tax-free income from home rental.

A tax-free rent strategy that allows the corporation to pay rent directly to the business owner, thus lowering the income passed through to the shareholder/owner, yet does not increase the personal taxable income reported on the individual return of the owner.

How does this work?

When an employer uses his/her principal residence to hold employee meetings, trainings, board meetings, customer/client demonstrations or dinners, a company Christmas party, or any other work function --- the owner can charge the corporation/LLC rent for the use of the premises.

Why does this work?

This works because it is customary to hold business meetings outside the regular business location. Often employee training is held off-site because it gets employees away from their regular work site. Clients and patients are almost always promoted outside the office/business location. Company events/parties are rarely at the office.

And because casual rent (for 14 days or less per year) is not considered taxable income per IRS stipulation (available upon request)

Tax Result:

Hotel costs for the use of a business room are expensive. Add catering, and it's even more costly. Each event would cost the business at least $1000 for a few employees, and likely $1500-$2000 depending on the number of total attendees.

Use the home just 10 times instead of the total allowed 14, and the amount can easily be

$12,000 to $15,000. At a 35%-40% federal and state tax bracket, that's a tax savings of around $5000 or more per year. It could often be more than that.

2) **Incorrect vehicle strategy. A properly established and correctly reporting vehicle strategy that allows the corporation to write-off 100% of the vehicle use.**

How does this work?

When you use a vehicle for business in a sole proprietorship, you are required to allocate the business versus personal use by keeping a mileage log of business activity. This results in a portion of the vehicle expenses being written off.

Under the corporate structure, the corporation would own the vehicle and provides it to the employee (you) in order to be used to accomplish business tasks, and for your convenience when needed for personal use. In this scenario, the corporation writes off 100% of the vehicle, its costs, all expenses, etc. because the corporation has no personal use of the vehicle.

However, whenever an employee uses a company vehicle for personal use, the company reports that personal use on the employee's W-2 in order that the employee will be taxed on it as compensation.

In fact, the IRS has written regulations that present several options for the closely held corporation (that's an incorporated small business like yours) to report such income on the owner-employee's W-2. Of course, we take the best option for your best overall tax benefit. You can find this elaborate information in IRS Publication (available upon request).

Why does this work?

This works simply because the 100% write-off enjoyed by the corporation is much more than the personal use income reported on the owner-employee's W-2 – thus creating a deduction greater than the split percentage method required by the IRS when the vehicle is used for business within a sole proprietorship.

Tax Result:

Taking 100% of the vehicle expenses as a deduction can create several thousand dollars of additional deductions in excess of the owner-employee W-2 income. Usually it's at least $3000-$8000 in additional write-offs. For larger vehicles over 6000#s, the tax benefit is significantly greater. With the current tax law, this deduction is even better.

This one item alone saves an average of around $2,500 per year in taxes for my clients, and it's often substantially more than that.

3) **No family employment. The employment of children in the family business is a tremendous opportunity for a tax break and to teach your offspring responsibility.**

Every US person can have earnings up to $12,950 (as of this writing) without being taxed (even if the person is claimed as a dependent by a parent). And this amount goes up each year, although you probably won't use up that much.

And for children under 18, there is no social security/Medicare withholding to be taken, and there is no payroll tax to you.

But if you pay your children for service performed out of your corporation you do NOT avoid paying the associated payroll taxes, and you cannot avoid withholding social security and Medicare from their pay. Learn how to avoid that trap by contacting our office.

4) No Health Savings Accounts.

HSAs are ideal for most business owners because they tend not to use medical doctors often. These high-deductible plans are much more affordable than standard plans, still provide a tax deduction for the premium paid, and offer an opportunity to both put money away for retirement and convert non-deductible medical expenses to tax write-offs.

How does it work?

Medical deductions on your Schedule A as itemized deductions just don't add up to much. You only get the deductions for the amount each year that exceeds 7% of your total income. That means for a taxpayer earning $100,000, the first $7,000 is not deductible as an itemized deduction.

You're not going to get a good tax deduction that way.

Thus, Congress passed the Health Savings Plan tied into your medical insurance. It's a high deductible plan, designed to cover only major medical stuff.

The other advantage is that you are allowed to place funds into the HSA up to the amount of your deductible – $7,800 per year (and it tends to go up annually) for a family (50% of that for singles)

-- and it is tax deductible. You can pay for out-of-pocket medical expenses from this special account, making the medical bills deductible. If you don't use the funds, the savings accounts functions like an IRA and can be saved for future retirement.

Tax Result:

The HSA tax deduction creates a tax savings of around $3,000 per year or more.

Important note: And you are allowed to make this contribution all the way up <u>until April 15 of the next year.</u>

And if you're over 50, add $1,000.

{If cash flow may not allow this payment all at once, see our advisors for a trick to fund this HSA in full every year!}

5) Incorrect low deduction of food costs.

The opportunity for employer-provided meals is often neglected, which is particularly helpful to business owners who return after 5PM or stay during lunch to serve patients, customers, doctors and or other professionals.

6) No payroll strategy for the business owner and/or spouse; missing savings of thousands in deductions and payroll tax savings.

Nearly every new business client we talk to does not have the correct amount of payroll, and no payroll strategy.

Save at least hundreds, possibly thousands in payroll taxes.

7) Failure to take the home office deduction.

Nearly every business owner uses an office at home for a place to study, make business plans, or perform substantial administrative work.

Business owners work at home. Sometimes it is the best place for thinking (planning)as well. You get a deduction for that; it's that simple — And it's a solid write-off backed by Congress (if you want to hear about the congressional history of this bona-fide and solid deduction, just ask!)

And because you have 2 business locations, automobile deductions are escalated.

Learn how to take the full home office deduction without the home office form even appearing on your tax return.

8) Improper compensation to spouse. Most spouses work in or assist with the business in some way. You have two major options with regard to 'employing' your spouse – and the results will equal thousands of dollars in tax savings each year if you do it right.

There are a few options within this strategy – one to fit every business owner to accumulate thousands more in tax deductions that are codified in several places under the Internal Revenue Code.

9) No real estate. If you have real estate, keep it. If you don't own any, buy it.

If you have the capacity, buy more. If you don't yet have the capacity, plan to get it. No tax plan should be without a real estate investment plan. This is true if you are starting out, or if you are well established. Start with a single-family rental, your own home, or buy a commercial spot for your business. The SBA is lending and provides you a great option.

10) You have a real estate LLC, but the kids are not in it.

Children may own the tiniest portion of a real estate LLC, yet be allocated up to $2,000 each annually in real estate income, without taxation.

It's incredible what Congress has done for its special interest groups, and in its attempt to continue to spur the economy. And you can include yourself in it.

Let's add up (conservatively) just the things in this article that you might hope your accountant would tell you, and see what it comes up to:

Tax-Free Rent Deduction	$9,000 (or more?)
Corporate Vehicle 100% Deduction	$5,000 (or more?)
Pay Your Children	$8,000 (or more?)
Health Savings Account	$7,800
Home Office Deductions	$5,000 -7,000 (or more?)
Employer Provided Meals/Other	$2,000
Spouse Working for the Business	$4,000 -10,000 (or more?)
Children in Real Estate LLC	$2,000 -10,000 (or more?)
Real Estate Depreciation	$10,000 – 20,000 (and more?)

[this amount is for one $350K single family home. So that would be more in many locations]

That is about $70,000 or more in tax deductions every single year, and that's just from the above items, and somewhat conservatively.

Fortunately, you save tax at your 'marginal' tax bracket – the rate at which your last-earned dollars are taxed.

If you make more than around $90,000 taxable, that is 24% federal (plus whatever your state tax rate is).

If you make more than $216,000 taxable, that is 35% federal [plus state. (CA,HI,NY,OR,MN,IA,NJ,VM all hover around 10% or more at this income level)]. That's 45%!

Add the 3.8% net investment tax, and the 1% extra Medicare tax if over $250,000 married, $125,000 unmarried, and…… whew!

Most business owners are at a marginal tax bracket of 35-40% or more overall.

Many of you reach toward or over 50%!

You can easily do the math for what these $70,000 in new deductions will do for you every year. Get with a Records In Order consultant today. Go to RecordsInOrder.com!

- **Scott C Turner, CPA**