MONEY MATTERS

YEAR-END TAX PLANNING

By Jacob Ansel

YEAR-END TAX PLANNING PRESENTS the opportunity to explore ideas that can maximize tax savings and help small business owners keep more net income and profits. In 2015, small businesses saw an uptick in sales and net profits which means now is the perfect time to take a look at pending tax liabilities and find a way to decrease taxes.

If you own a majority of your company and have young children, consider putting them on the payroll which will save you on FICA tax and reduce income tax. Income for a child is taxed at a lower rate. Consider a $5,000 payroll for each which also provides a good opportunity to teach them how to save and invest for the future. Put that $5,000 in a company 401(k) plan so they can start investing from a young age.

Pensions are the single smartest tax planning tool and a great way to reduce taxes for most small businesses. If your profits are high and you have good cash flow, consider a 401(k) plan with a profit sharing feature as well as a defined benefit plan (DBP). The limit for a 401(k) plan contribution for 2015 is $18,000 if you're under 50; $24,000 over 50. Add to that a profit sharing feature which is 6% of compensation and a DBP and you can really reduce your tax bill. The defined benefit is actuary determined based on salary, age, and other factors and the tax deduction for a DBP can be huge and shouldn't be overlooked.

Year end purchases of computers, equipment, and furniture are smart ideas. The deduction for these purchases is set to roll back to $25,000 for a one-time write off. (That pales in comparison to past write-offs of $500,000.) Even though this provision is set to expire, it shouldn't be discounted. A $25,000 one-time tax deduction plus regular depreciation on your assets adds up.

Deferring your income is a popular way to reduce income and taxes. If you need to do this delay sending out invoices to customers. If you're having an unusually exceptional income year and are looking for ways to reduce income but don't want to contribute more to a pension, deferring income to 2016 is a smart move.

On the other hand, if you had a pretty bad year with a lower than average profit and expect your profit to pick back up next year, you may want to defer as many expenses as possible. If you're in the 20% tax bracket this year, but will be in the 30% tax bracket next year and you have $10,000 worth of expenses in question, deducting them this year will save you $2,000, while deducting them next year will save you $3,000. Make sure you know whether you file your tax return on the accrual basis or the cash basis. Most year-end tax strategies only work for cash-basis taxpayers. Accrual-basis taxpayers report all income in the year that it's earned and all expenses in the year that they're incurred. So, just because you're paying for a 2015 expense in 2014, it doesn't mean you get to deduct that item in 2014.

Have your accountant prepare an estimated or mock tax return. Most CPA firms use a program called BNA that can easily prepare estimated tax returns, extremely useful for planning purposes. How much should we spend on bonuses, pensions, equipment, planned purchases, taxes? The best way to know is to paint a few scenarios for the client. Knowledge is power and having the information in advance of year end helps in planning.

Be aware of federal and state income tax rates for your income level. The top federal tax bracket for 2015 is 39.6% when income is higher than $464,850 (married filing jointly) or $413,000 (single).

Don't spend money that you wouldn't ordinarily spend just to reduce your tax bill. Remember, $1 spent doesn't equal $1 worth of tax saved: $1 spent creates a $1 deduction, which (depending on your tax bracket, business structure, and state of operation) will only lead to $.00 to $.60 worth of tax saved.

You should review your income and expenses monthly and meet with your CPA or tax advisor quarterly to analyze how you can take full advantage of the provisions, credits, and deductions that are legally available to you. ❑

Many small business owners ignore tax planning and don't even think about their taxes until they're scheduled to meet with their accountant. Tax planning is an ongoing process and good tax advice is a valuable commodity which you shouldn't wait until the last minute to get.

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