

7 Top Tax Strategies for Business Owners

By: David Talley, CFP®, EA



TALLEY
FINANCIAL

1. Choose the Right Entity Type

As a business owner, one of the crucial decisions you'll face is [selecting the right entity type for your company](#). Whether you are considering an LLC, sole proprietorship, S-corporation, C-corporation, or partnership, this decision can have a significant impact on your tax liability and overall financial well-being. Selecting the appropriate entity type can lead to substantial tax savings by minimizing self-employment taxes and leveraging retirement plan options.

Understanding the Impact of Entity Type on Taxes

Choosing the right entity type can open up a world of tax-saving opportunities as your business grows. It goes beyond just federal and state income taxes; it also affects self-employment taxes, payroll taxes, retirement plans, and overall tax savings strategies.

For example, transitioning from a sole proprietorship to an S-corporation can result in substantial tax savings. By paying yourself a reasonable salary as the owner and classifying the rest of the profit as dividends, you can avoid self-employment taxes on a significant portion of your income.

Maximizing Tax Savings through Strategic Entity Type Selection

The key to maximizing tax savings lies in understanding the nuances of each entity type and how they impact your tax liability. Working with financial planners, CPAs, and attorneys can help navigate the complexities of changing your entity type and ensure that you are making the most tax-efficient choice for your business.

[Choosing the right entity type](#) is not just a legal decision; it's a strategic tax-saving move that can result in significant savings for your business. By proactively evaluating and selecting the entity type that aligns with your financial goals, you can set your business up for long-term success and maximize tax efficiency.

2. Choose the Right Business Retirement Account

Exploring options like 401(k)s, SEP IRAs, solo 401(k)s, and profit-sharing plans can help business owners set aside funds for retirement while deferring taxes to a later date. Selecting the right business retirement account is key to long-term financial security.

Understanding Your Options

The array of [retirement account options](#) can seem daunting, but each serves a unique purpose based on your business needs, profits, and long-term financial goals. By selecting the right account, you can effectively set aside income and defer taxes to a more favorable time in the future.

Maximizing Tax Benefits

Choosing the correct business retirement account has one significant advantage: the ability to reduce your current tax burden by deferring income to a later date. If you find yourself in a high-income bracket now, opting for a retirement plan that allows for deferral can lead to substantial tax savings in the future when you may be in a lower tax bracket.

Cash Balance Plans

Cash balance plans stand out among the various retirement account options available for their ability to accommodate substantial contributions, making them an attractive choice for business owners aiming to defer a significant portion of their income. With the potential to defer hundreds of thousands of dollars annually, cash balance plans offer a powerful tax-saving opportunity for high-income business owners.

3. Consider Hiring Family Members

By hiring your spouse or children in your business, you can transfer income to family members in lower tax brackets, potentially reducing your tax liability. Paying reasonable salaries to family members who contribute to the business can be a tax-efficient strategy. While this may sound simple, there are key considerations to keep in mind to make the most of this opportunity. The crucial aspect to remember is that your kids must

genuinely contribute to the business. Simply deciding to pay them without them actually working won't cut it.

Tax Benefits of Hiring Kids

If your kids are capable of performing tasks, even small ones, you can pay them up to the standard deduction amount. You can then allow them to file a single filer tax return. For example, if you paid them \$14,000 in a year, that \$14,000 shifts from taxable income for you to tax-free income for them. This is because they automatically receive the standard deduction.

By employing your kids and paying them for legitimate work, you can shift income from being taxable to entirely tax-free. Achieving a 0% tax rate is as good as it gets in terms of tax savings. Moreover, this opens up opportunities to invest money for them in tax-free accounts like a Roth IRA, providing long-term financial benefits.

Eliminate Tax Dollars Strategically

Utilizing this tax-saving strategy helps you eliminate tax dollars and enables you to secure your family's financial future. By diverting income to your kids and leveraging tax-free investment options, you can set them up for financial success while reducing your tax burden.

Hiring family members can be a powerful tax strategy for business owners. By following the right guidelines and ensuring that your family members are genuinely contributing to the business. Implementing this strategy benefits your business financially and strengthens your family's financial stability in the long run.

4. Take Advantage of an HSA

Business owners are always looking for ways to minimize their tax burden and maximize their savings. One often overlooked but powerful strategy is leveraging a Health Savings Account (HSA). Not everyone may have access to an HSA, but if you have a high deductible health insurance plan, funding an HSA can be a game-changer in your tax planning.

Why Choose an HSA?

An HSA provides immediate tax benefits, unlike traditional retirement plans that defer taxes to the future. When you contribute to an HSA, you enjoy a tax deduction on the amount you put in, effectively reducing your taxable income. Even better, the funds in

your HSA grow tax-free, and as long as you use them for qualified medical expenses, you never pay taxes on them. Yes, you heard that right – you can potentially be in a 0% tax bracket when it comes to your HSA contributions and withdrawals.

Long-Term Benefits of HSA

Imagine maxing out your HSA contributions every year from a young age. By the time you reach retirement age, you could have accumulated a substantial balance in your HSA, all shielded from taxes. Medical expenses are almost inevitable for most individuals or their family members at some point in life, making an HSA a valuable tool for building a tax-free nest egg for healthcare costs.

Taking advantage of an HSA is not only about saving on taxes today. It's a strategic long-term investment in your health and financial well-being. By funding your HSA, investing the contributions, and using the funds for qualified medical expenses, you can enjoy significant tax savings and financial security for the future.

5. Accelerate or Defer Income.

Strategic income timing can play a significant role in managing taxes. By deferring or accelerating income based on your current tax situation, you can optimize your tax position and potentially lower your overall tax burden. Understanding your income fluctuations and tax brackets is essential for effective tax planning.

Accelerating Income

When you're experiencing a high-income year, it might be advantageous to accelerate your income. By doing so, you can take advantage of lower tax brackets in future years. This means bringing in income that you would typically receive in the following year into the current year. This can be particularly beneficial if you foresee your income decreasing in the near future or if you had a down year due to business losses.

Deferring Income

Conversely, if you're currently in a lower tax bracket or anticipate a decrease in income, deferring income can be a smart move. By postponing income to future years, you can potentially pay taxes on that income at a lower rate. Utilizing retirement plans and prepaying expenses at the end of the year are effective ways to defer income and reduce your current tax burden.

Tax Timing is Key

Many business owners overlook the significance of tax timing in their financial planning. The ability to control when you receive income allows you to navigate tax brackets strategically. Whether it's shifting income to the current year to benefit from a lower tax bracket or postponing income to reduce tax liabilities, understanding and leveraging tax timing can have a substantial impact on your overall tax situation.

Business owners can proactively manage their tax obligations and potentially save significant amounts of money by mastering the art of accelerating or deferring income. Work closely with a tax professional to develop a personalized strategy that aligns with your financial goals and circumstances. Remember, with taxes, timing is everything.

6. Donate to Charity

Donating to charity is a well-known method to receive a tax deduction. However, the ability to use various strategies to maximize your deductions sets it apart. One such method is through a donor-advised fund. Using tools like donor-advised funds and appreciated securities can optimize your charitable giving strategy and maximize tax deductions, all while making a positive impact.

Donor-Advised Fund

You can manipulate the timing of your donations to align with when the IRS recognizes them by utilizing a [donor-advised fund](#). This flexibility allows you to optimize your deductions, especially during high-income years. Consider contributing multiple years' worth to a donor-advised fund in a single year to capitalize on a substantial itemized deduction without wasting the standard deduction in the future.

Charitable Remainder Trusts and Appreciated Securities

Another valuable strategy is to explore charitable remainder trusts and donating appreciated securities. When you donate appreciated assets like securities or real estate, you not only support a cause but also avoid capital gains tax. By gifting appreciated assets instead of cash, you can implement a tax-efficient strategy that benefits both you and the charitable organizations.

Incorporating charitable donations into your tax planning can provide significant benefits beyond the satisfaction of giving back. Business owners can optimize their financial outcomes while supporting causes they care about by understanding and utilizing these tax strategies effectively.

7. Real Estate

Real estate investment can be a powerful tool for business owners looking to optimize their tax strategies and secure long-term financial stability.

Cost Segregation Studies

One of the most impactful strategies mentioned is the use of cost segregation studies to accelerate depreciation on real estate purchases. By conducting a thorough analysis, business owners can potentially deduct a significant portion of their property's value in the current year, rather than spreading it out over a longer period. This not only reduces taxable income but also provides substantial deductions.

Renting Personally Owned Real Estate to Business

Renting personally owned real estate to your business can yield significant tax benefits. Business owners can deduct the rent paid by the business as a legitimate business expense by establishing a rental agreement, reducing taxable income. This often overlooked strategy can result in substantial deductions without additional financial outlay.

Real estate offers a myriad of tax advantages for business owners willing to navigate the complex rules and regulations. There are numerous strategies available to minimize tax burdens and maximize returns on real estate investments.

Incorporating these top tax strategies into your business planning can use the power of real estate to build wealth, reduce tax liabilities, and secure a financially sound future for your business.

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