

Here are Some Year-end Tax Tips

Many of the provisions of the 2001 Tax Act go into effect in 2002. With year end around the corner, let's explore some strategies where small business owners can minimize this year's tax bite.

Income Recognition

Cash basis taxpayers can benefit from IRS rules by steering income recognition to the more beneficial year, if the business has control over billings, cash receipts and determination of bad debt accounts receivable. Officer and employee bonuses can be paid at year end, or if necessary, deferred to next year if more beneficial for business financial and tax considerations.

Expense Timing

Businesses can accelerate tax write-offs by paying bills by December 31 (rent, utilities, taxes, etc) even if they are not due until January. Individuals can apply this technique on their personal tax return, and an extra month end mortgage payment could result in more deductible interest for 2002. Winter property taxes normally due in February should be paid by year end, if possible. Taxpayers who are borderline itemizers (versus standard deduction) can use the bunching method (medical expenses, property taxes, charitable contributions, etc) to maximize IRS allowances.

Retirement Planning

Qualified and non-qualified retirement plans should be utilized to save current tax dollars and provide future benefits to employers and employees alike. Simple IRAs and SEP IRAs are less costly than 401(k) plans and should be considered in year end planning decisions. SEPs and SIMPLEs don't provide as much deferral as 401(k), but non-qualified plans could be supplemented to provide additional retirement benefits.

Education Planning

Employer provided educational aid allows for a \$5,250 exclusion from income to the employee as a tax free fringe benefit under the current law. The qualifying expenses now include graduate courses in addition to classes that need not meet the minimum requirements of the job. Individual taxpayers should take advantage of increased limits of Coverdell (educational) IRAs and their expanded expenditure usage. Hope Scholarship and Lifetime Learning Credits, as well as above the line tuition and student loan interest deduction, should be considerations with individual income tax planning.

Choice of Business Entity

Many small businesses do not explore the various choices of IRS business tax recognition when they initiate operations. The current trend toward LLC (Limited Liability Company) should be considered for owner personal liability consideration. S corporations offer alternative tax benefits and are popular choices for business choice of entity.

Family Member Income Shift

Self employed business owners avoid self employment tax (FICA, Medicare) on monies paid to minor children who perform significant duties for the business operation. Children and other family members who are in lower tax brackets will benefit by becoming shareholders of an S Corporation, whom will also benefit by less social security burden.

Medical Expense Reimbursement

Tax-free fringe benefits can be lucrative in that they are utilizing pre-tax dollars. A medical reimbursement plan can be formalized to include qualifying employees' medical expenses that are not otherwise covered by insurance, or deductible on the individual form 1040.

Home Office Deduction

Many small businesses operate from a home-base. To that extent, deductions may be taken for a home office that serves as the principal place of business. Care should be taken in how the expenses are reflected on the respective business tax return, in order to avoid possible tax, upon sale of the personal residence.

Equipment Acquisition

The Economic Stimulus Bill of 2002 created bonus depreciation for new asset acquisitions. The Section 179 deduction, or direct expensing, remains at \$24,000 allowable for 2002. Caution - Partnerships and S Corps can expense new equipment only to the extent they have taxable income.

The dreaded task of tax filing can be made less painful with proper tax planning and timely attention to alternative options. It is extremely beneficial for the business owner to maintain timely and open communications with the CPA in order to maximize available benefits. As always, I welcome your thoughts, questions and comments.

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