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Certified Public Accountant · Business Advisor

Tax-Saving Tips

Issue: 1

May 15, 2017

Corporate Tax Break for Your and Your Employees' Smartphones and Tablets.

When a corporation provides an employee or a partner with a smartphone or similar telecommunications equipment primarily for non-compensatory business reasons, the employee or partner receives a tax-free fringe benefit. The tax-free part works like this: the employee's or partner's business use is a working condition fringe benefit that is excludable from taxable income, while the personal use is a de minims fringe benefit that also is excludable from taxable income. And to top it off, the employee or partner does not have to keep any records of business use.

To see how this works in action, let's say you operate your business as an S corporation. The corporation decides to provide you with the smartphone fringe benefit. You use the phone about 15 percent for business and 85 percent for personal purposes. Your annual cost for the phone is $1,260. You benefit as follows:

- Your S corporation reimburses you $1,260 for the smartphone use (cash in your pocket without taxes).
- Your S corporation deducts the $1,260 and passes that tax deduction to you via Schedule K-1. In your 40 percent tax bracket, you realize an additional $504 in cash from this deduction ($1,260 x 40 percent)

Using a 529 Plan to Pay for Your Child's College

A Section 529 plan is a great way to fund your child's college education. For income tax purposes, it works like this:

- no tax deduction for the money you put into the plan,
- tax-free growth inside the plan, and
- tax-free distribution when the money or prepaid tuition is used for college.

For gift-tax purposes, the 529 plan works like this: contributions to 529 plans are taxable gifts eligible for the annual gift-tax exclusion of $14,000 per donee (2017 amount), which doubles to $28,000 if your spouse consents to gift splitting.

The tax code contains a special option for 529 plans that allows you to spread the contribution over a five-year period so you can take advantage of the $14,000 annual exclusion. For example, you can contribute $70,000 to the 529 plan and use five years of the $14,000 exclusion to avoid any gift taxes. You and your spouse, with combined consent, could contribute $140,000 and use the five-year rule to avoid gift taxes.

Win-Win with Length-of-Service Awards

There's really nothing more valuable to a business than good employees, particularly those who stick with you for years and years. One way to honor those longtime employees is to give them a meaningful present or award. The tax code includes a special carve-out for "employee achievement awards," which means that when you buy

something for your employees in recognition of their years of service, you get a tax break—and your employees do too. You can deduct the cost of the gift, and the employee pays no tax on it.

You can give the length-of-service award to an employee every five years. That is, an employee must have worked for your company for at least five years before you can give him or her one of these awards, and you have to wait at least five years before you can give that same employee the next such award.

So, what kind of award qualifies? There are four requirements:

1. **Tangible property.** The award must be tangible property—not cash or a cash equivalent. Think things like watches, cookware, and televisions.
2. **Meaningful presentation.** You must give the award during a "meaningful presentation." That doesn't mean you have to put up streamers and serve champagne, but you should have some sort of "ceremonious observance" in which you recognize your employee for his or her service.
3. **Deduction limit.** In general, tax law limits the deduction for achievement awards to no more than $400 per employee per year.
4. **No disguised compensation.** You can't cut the employee's salary to make up for giving a tax-free achievement award, nor can you give the award as a disguise for normal compensation.

Tax-Free Income from Rental of Your Home to a Corporation

IRC Section 280A allows you to rent your entire home tax-free for 14 days or less during the year: no tax on the income, and no deductions for the home. You can rent to a third party or to your S or C Corporation. For example, say the fair rent on your home is $1,500 a day and you rent the home to your corporation for 14 days during the year. Here's how you benefit:

- The S corporation deducts the $21,000 ($1,500 x 14) and passes the benefits of that deduction to you. If you are in the 40 percent tax bracket, your cash benefit is $8,400 ($21,000 x 40 percent).
- You also receive the $21,000 in rental income tax-free, for a total cash benefit of $29,400 ($21,000 + $8,400).

You have to admit, this sounds almost too good to be true. But it is true. This result is embedded in the law, and it's available to you if you operate your business as an S corporation. (The C corporation produces slightly different cash results.)

Tax Law Favors Corporate Debt over Equity

If you decide to use a C corporation to operate your newly acquired business, you should know that our current federal income tax system treats corporate debt more favorably than corporate equity. So including some third-party debt (owed to outside lenders) and/or some owner debt (owed to yourself) in your corporation's capital structure is a tax-smart move.

Even if you could afford to cover the entire cost of the new business with your own money, tax considerations may make this inadvisable. That's because a C corporation shareholder generally cannot withdraw part of his or her equity investment without worrying about the dreaded double taxation issue. If the corporation has current or accumulated earnings and profits, all or part of the withdrawal will be treated as a taxable dividend. You want to avoid dividends if you can. Taxable dividend treatment means taxable income for you without any offsetting deduction for your corporation—that is, after your corporation has already been taxed on its profits. This is double taxation in all its glory.

When third-party debt is used in your corporation's capital structure, it becomes less likely that you will need to be paid taxable dividends. The corporation's cash flow can be used to pay off the debt, and when the debt is paid off, you will own 100 percent of the corporation with a smaller investment on your part.

We Are Here for You

As always, we are at your service. Should you desire our assistance in implementing any of the ideas in this newsletter, please don't hesitate to contact us.