

## HIRING CHILDREN OR FAMILY MEMBERS IN THE COVID-19 ERA

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Many small businesses have been hurt by the COVID-19 crisis. That's not news. What has not changed is seeing what techniques should at least be explored to so keep taxes down, to keep more of your hard earned money intact.

We often suggest to our closely held business owners they consider hiring one or more of their children or other family members to work in their business. In this financially challenging COVID-19 era, that can be a good idea—if for no other reason than it keeps money in the family where it may be sorely needed. There is an array of tax benefits that can come along with hiring a child or family member. The tax benefits can be significant. This could help their family and their practice/business overcome COVID-19-caused cash-flow challenges while also delivering favorable tax results to both the newly-employed family members and the businesses that hire them. Of course, the wages must be reasonable for the work performed.

### SOLE PROPRIETORSHIPS AND HUSBAND-WIFE PARTNERSHIPS CAN HIRE UNDER-AGE-18 CHILDREN

If you operate your business as a sole proprietorship, a single-member LLC that's treated as a sole proprietorship for tax purposes, husband-wife partnership, or LLC that's treated as a husband-wife partnership for tax purposes, you can hire your under-age-18 child as a legitimate employee, and the child's wages will be completely exempt from Social Security and Medicare taxes (FICA tax) and Federal Unemployment Tax (FUTA tax).

The FICA tax exemption applies to both the employee's share of FICA tax that's withheld from his or her paycheck and to the employer's share of FICA tax. So, both the employee-child and the business come out ahead. Note that the FUTA tax exemption lasts until the employee-child reaches age 21.

You can hire an under-age-18 child part-time, full-time, or whatever works for the business and the child's schedule. Will the child go back to attending school in person in August or September, or will classes be conducted online? You may not yet know for sure, but the child's availability to work in the business may be at an all-time high in the COVID-19 era.

Wages received by your child can be used to help keep the family afloat financially. If your family is not so financially stressed, the child can use some or all of the wages to fund a college savings account or make an IRA contribution (traditional or Roth). Note that the child must have earned income during the year to make an IRA contribution. The maximum IRA contribution for the 2021 tax year is \$6,000 for anyone who will be under age 50 as of 12/31/21. If your child contributes to a traditional IRA, he or she could earn up to \$18,550 in 2021 without paying any income taxes (\$12,550 standard deduction plus a \$6,000 deductible IRA contribution).

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## ARE THE TAX RESULTS STILL GOOD WHEN AN OLDER CHILD IS HIRED?

Yes, but if the newly-employed child is age 18 or older, his or her wages are subject to FICA tax, just like for any other employee (21 for FUTA tax). From an income tax perspective, the results are even better. For 2021, your child will owe no federal income tax on the first \$12,550 of wages received from the business if he or she files as a single taxpayer and has no taxable income from other sources. That amount increases to \$18,650 if the child files as head of household or \$24,800 if married filing jointly. This is true regardless of the child's age, thanks to the standard deduction.

## ARE THE TAX RESULTS STILL GOOD FOR AN INCORPORATED BUSINESS?

Yes. If you operate a business as an S or C corporation, the child's wages received from the business are subject to FICA and FUTA taxes, just like for any other employee, regardless of the child's age. However, here's the good part. For 2021 your child will owe no federal income tax on the first \$12,550 of wages received from the business if he or she files as a single taxpayer and has no taxable income from other sources. That amount increases to \$18,800 if the child files as head of household or \$25,100 if married filing jointly. This is true regardless of the child's age.

## ENSURING THE TAX ADVANTAGES FOR YOUR BUSINESS

Hiring a child or other family member to work in your business can be a smart move in the COVID-19 era. However, we strongly suggest that clients who follow through with this idea must do the following:

1. Pay reasonable wages for the work performed to lock in tax-saving expense deductions. Higher wages can be paid to children or family members who are teenagers or older because they can be assigned to more-meaningful tasks.
2. Keep payroll records just like for any other employee to document hours worked and duties performed (e.g. timesheets and job descriptions).
3. Issue W-2s just like for any other employee.

### For more information, contact:



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