

# Tax Saving Strategies for Small Businesses

SCORE GREATER SEATTLE CHAPTER

Version: 22 March 2025 - Online  
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## Objectives of the Workshop

**Help you learn about:**

- The key 10 tax saving strategies for small businesses – that really work.
- Real life examples of how other small businesses have implemented these strategies to save them big money.

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## 83% of Americans Overpay Their Income Taxes

**Why?:**

- Belief that taking all deductions will increase chance of audit.
- Belief that, if audited, will be able to show other deductions not taken to offset additional taxes.



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## Your Presenter


**Joe Heinrich**

Volunteer with SCORE:

- Small Business Mentor since 2011, with expertise in Finance, Accounting and Taxes
- Workshop Instructor

Previously:

- VP Finance with Coca-Cola Enterprises Inc. for 21 years
- CPA with KPMG, international accounting firm for 11 years
- Retired since 2011



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## Introductions

Introduce yourself using the chat function, stating the following attributes about yourself:

- Your first name
- The industry your business is in, or a very short description of your business.



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## SCORE's Business Success Resources

**SCORE**


- Our mission is to foster vibrant small business communities through mentoring and education.
- National non-profit organization with 300 chapters and 10,000 volunteers.
- Greater Seattle Chapter has over 100 volunteers with a variety of different backgrounds and expertise.

**SCORE Mentors**

- Meet one-on-one with expert business mentors in many business specialties. Mentors advise, educate and encourage business owners to help them develop and be successful in their businesses.
- Register for mentoring at <https://www.score.org/seattle/local-mentors>

**SCORE Small Business Workshops**

- Register for workshops at <https://www.score.org/seattle/local-workshops>



**SCORE Website**  
Information, business plan templates, newsletters, etc.  
Online webinar training  
<https://www.score.org/seattle>

**SBA Website**  
<https://www.sba.gov/offices/district/wa/seattle>

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## Sponsored by GDM Private Financial Solutions



GDM Private Financial Solutions is a highly skilled Bellevue, WA CPA firm offering innovative accounting services and tax planning solutions for small business owners. Our mission is to remove financial obstacles and skillfully manage your tax obligations to improve your business and your bottom line.

At GDM Private Financial Solutions, we understand the difficulties behind choosing the right CPA for you or your business, which is why we offer a **free initial consultation**. This allows you to get to know us and us to get to know your business - so we can build a long-term professional relationship.

Give us a call today at **425-283-5425** to schedule your **free initial consultation**.

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## Workshop Agenda

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|---|---|
| <ol style="list-style-type: none"> <li>1. Federal Taxes and Taxing Regimes</li> <li>2. Minimizing Federal Taxes             <ol style="list-style-type: none"> <li>a) S-Corporation Election</li> <li>b) Business Use of Home Deduction</li> <li>c) Business Use of Personal Vehicle</li> <li>d) Saving for Retirement</li> <li>e) Saving for Health Costs</li> </ol> </li> </ol> | <ol style="list-style-type: none"> <li>f) Saving for School and University Tuition</li> <li>g) Purchases of Equipment</li> <li>h) Maximizing Deductions</li> <li>i) Tax Credits for Businesses</li> <li>j) Cash vs. Accrual Accounting</li> <li>3. Concluding Comments</li> </ol> |
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## Enjoying the Workshop

- Participation is encouraged!!
    - Ask questions as we go. Use the "Hand Raise" button to ask questions.
    - Learn from your instructor and the other participants.
  - Handouts and electronic versions.
  - We may not have time to fully resolve every question so, see please feel free to send me an email with your questions!
- joseph.heinrich@scorevolunteer.org

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## Workshop Agenda

1. Federal Taxes and Taxing Regimes
2. Minimizing Federal Taxes
  - a) S-Corporation Election
  - b) Business Use of Home Deduction
  - c) Business Use of Personal Vehicle
  - d) Saving for Retirement
  - e) Saving for Health Costs
3. Concluding Comments
  - f) Saving for School and University Tuition
  - g) Purchases of Equipment
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## Federal Taxing Regimes

All of us pay Federal Personal Income Taxes under one set of laws, or one taxing regime.

However, the Federal Government taxes businesses under a variety of different taxing regimes, depending on the regime that is most suitable or is chosen by the business.



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## Key Federal Taxing Regimes for Small Businesses

There are four key Federal taxing regimes for small businesses:

- Sole Proprietorship
- Partnership
- S Corporation
- C Corporation



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### Taxing Regime Choices for Small Businesses that are Not Legal Entities

If the business has only one owner:

- Sole Proprietorship

If the business has more than one owner:

- Partnership



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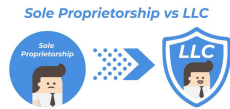
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### Benefits for Creating a Legal Entity for Your Small Business

There are two main benefits for creating a legal entity for your business:

- Legal liability protection for yourself and your family if your business gets sued.
- Provides you a choice of Federal taxing regimes, of which one may be more advantageous to you for saving taxes.



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### Key Washington For-Profit Legal Entities for Small Businesses

There are three key Washington corporate legal entities for small businesses:

- Limited Liability Company (i.e., an "LLC")
- Regular Corporation (i.e., an "Inc.")
- Social Purpose Corporation (i.e., a "SPC")

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### Creating a For-Profit Legal Entity for Your Small Business

To create a for-profit legal entity in Washington, you need to make an application with the Secretary of State of Washington at the following website:

<https://www.sos.wa.gov/corps/all-services.aspx>

Cost is \$200 to create an LLC.  Secretary of State  
*Tim Wynn*  
Annual fee of \$70.

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### Federal Tax Regime Choices for a One-Owner Legal Entity Small Business

- ➔ Sole Proprietorship
- ➔ S Corporation
- ➔ C Corporation



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### Federal Tax Regime Choices for a Multi-Owner Legal Entity Small Business

- ➔ Partnership
- ➔ S Corporation
- ➔ C Corporation



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### Which Federal Taxing Regime is Best for Your Small Business?

In general, you and your business will save Federal taxes under the S Corporation taxing regime, if your business has taxable income (i.e., profits) in excess of \$70,000 annually.



We will discuss this in more detail in the next section of this workshop.

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### When Does the C Corporation Regime Make Sense?

In general, you and your business will pay more Federal taxes under the C Corporation taxing regime, due to the effect of the personal tax on dividends which are from previously taxed profits of the business (i.e., double taxation).

When to elect C Corporation status?

- ➔ Seek equity investments from numerous investors.

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### Key Federal Taxes on Small Businesses

There are three key Federal taxes on small businesses and their owners:

- Social Security and Medicare Payroll Taxes
- Unemployment Tax
- Personal Income Tax on Business Income



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## Social Security and Medicare Payroll Taxes

These taxes are imposed upon:

- Any business that has employees;
- All employees of that business;
- Owners of businesses that are considered "sole proprietorships" or "partnerships" by the IRS.



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## Social Security and Medicare Tax Rates

### Social Security Tax rate is:

6.2% on the first \$176,100 paid annually in wages to employees, paid equally by the employer and employee.

### Medicare Tax rate is:

1.45% on all wages to employees, paid equally by the employer and employee.

### Self Employment Tax rate is:

15.3% on the first \$176,100 of annual business taxable income and 2.9% on business taxable income in excess of \$176,100 if the business is a sole proprietorship or partnership, paid by the business's owner.



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## Example of Social Security, Medicare and Self-Employment Taxes on a Business

In 2025, ABC LLC had two employees, each earning \$50,000 in wages. ABC LLC had taxable income of \$60,000. ABC LLC, treated as a sole proprietorship by the IRS, is owned by Bob Long who works full-time on ABC LLC's business.

### ABC LLC pays:

\$7,650 in Social Security and Medicare Taxes on its employees' wages. (7.65% of \$100,000)

### Bob Long pays:

\$9,180 in Self Employment taxes on ABC LLC's taxable income. (15.3% of \$60,000)

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## Federal Unemployment Tax Rates

For 2025, the Federal Unemployment (FUTA) tax rate is 0.6%. The tax applies to the first \$7,000 you pay to each employee as wages during the year, which equals \$42 per employee per year.

However, if you are the owner of the business and you are considered an employee of your business, then the FUTA tax rate is 6.0% of the first \$7,000 of your compensation annually, or \$420.

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## Federal Personal Income Taxes

If the business is under the sole proprietorship, partnership or S-Corporation tax regimes, the owner(s) of the business pay Federal income tax on the business's profits (i.e., taxable income) using 2025 Federal personal income tax rates.

Unmarried			Married Filing Jointly		
Income Tax Rate	Taxable Income over	But not more than	Income Tax Rate	Taxable Income over	But not more than
10%	\$ -	\$11,925	10%	\$ -	23,850
12%	11,925	48,475	12%	23,850	96,950
22%	48,475	103,350	22%	96,950	206,700
24%	103,350	197,300	24%	206,700	394,600
32%	197,300	250,525	32%	394,600	550,050
35%	250,525	426,350	35%	550,050	751,600
37%	426,350		37%	751,600	

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## Federal Corporate Income Tax Rates

Incorporated businesses pay Federal Corporate Income Tax only if the business is taxed under the C Corporation taxing regime. In the event it is taxed as a sole proprietorship, partnership or S Corporation, the business pays no Federal Corporate Income Tax.

The Federal Corporate Income Tax rate 21% on all taxable income.

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## Workshop Agenda

- 1. Federal Taxes and Taxing Regimes
- 2. Minimizing Federal Taxes
  - a) S-Corporation Election
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  - c) Business Use of Personal Vehicle
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- f) Saving for School and University Tuition
- g) Purchases of Equipment
- h) Maximizing Deductions
- i) Tax Credits for Businesses
- j) Cash vs. Accrual Accounting
- 3. Concluding Comments

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## Objectives of Federal Tax Planning

- 1. Reduce your Federal taxes by employing strategies that permanently reduce your taxable income. These are tax "savings" strategies.
- 2. Reduce your Federal taxes by employing strategies that move taxable income from high marginal tax rate years to the same or lower marginal tax rate years in the future. These are tax "deferral" strategies.



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## Real Life SCORE Client Example #1

In 2015, hair salon owner implements the following tax saving and deferral strategies:

- 1. Creates LLC for her business
- 2. Elects S-Corporation status with IRS
- 3. Contributes \$12,500 to a SEP retirement Plan for herself
- 4. Takes a business use of home deduction.

Taxable income of business in 2015 (before owner's compensation) was comparable to 2014 before these tax strategies.



**Total reduction in 2015 taxes    \$11,557**

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## Real Life SCORE Client Example #2

In 2019, owner starts a computer consulting business and implements these tax saving and deferral strategies:

1. Elects S-Corporation status with IRS
2. Establishes a Solo 401(k) retirement plan
3. Took Deduction for Business use of the Home
4. Took Deduction for Business use of Vehicle



**Total reduction in 2019 taxes      \$17,292**

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## Use this Document to Track Your Ideas

Keep this document next to you during this workshop.

As we discuss each of the strategies, make a check mark in the "Implement" column if you feel this strategy is applicable to you or your business.

This will help you remember which strategies to follow up on later with your tax professional.

Implement Tax Strategy (check or initial)	Implement
1. Elect S-Corporation status with the IRS for your LLC	
2. Deduction for Business Use of the Home	
3. Deduction for Business Use of Personal Vehicle	
4. Saving for retirement using one of the IRS tax-qualified retirement plans	
5. Saving for out-of-pocket medical costs using a Health Savings Account (HSA)	
6. Saving for children's tuition	
7. Maximizing the deduction for meals, food and drinks and charitable contributions	
8. Claiming any Business Tax Credits that are available	
9. Making "Smart" equipment purchases	
10. What the method of accounting (cash vs. accrual) that will allow healthiest income flow	

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## Workshop Agenda

1. Federal Taxes and Taxing Regimes	f) Saving for School and University Tuition
2. Minimizing Federal Taxes	g) Purchases of Equipment
a) S-Corporation Election	h) Maximizing Deductions
b) Business Use of Home Deduction	i) Tax Credits for Businesses
c) Business Use of Personal Vehicle	j) Cash vs. Accrual Accounting
d) Saving for Retirement	3. Concluding Comments
e) Saving for Health Costs	

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## Benefit of S-Corporation Status

The benefit of electing S-Corporation status with the IRS is that you can split your business's taxable income into two parts:

1. Compensation to the owner(s) as an employee.
2. Net income of the business.

Thanks to this splitting, the owner(s) of the business will not pay Federal self-employment tax on the remaining net income of the business, permanently saving the Federal self-employment tax.

Sole Proprietorship	S Corporation
Total Income = \$75,000	Total Income = \$75,000
	Salary = \$37,500
	Dividends = \$37,500
Total Income	Salary
Self-Employment Tax = \$75,000 x 15.3% = \$11,475	Self-Employment Tax = \$37,500 x 15.3% = \$5,737.50

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## Rules on Electing S-Corporation Status

### Rules:

To qualify for S-Corporation status, the business must meet the following requirements:

- Be a domestic regular corporation or LLC;
- Have only allowable shareholders, including individuals, certain trusts and estates, and may not include partnerships, corporations or non-resident alien shareholders;
- Have no more than 100 shareholders;
- Have one class of stock; and,
- Not be an ineligible corporation i.e. certain financial institutions, insurance companies, and domestic international sales corporations.

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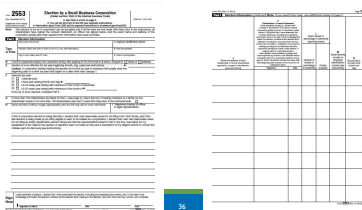
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## How to Elect S-Corporation Status

A corporation or LLC can elect S-Corporation status with the IRS by completing Form 2553 and submitting it to the IRS during the first 75 days of the business's fiscal year. Late filings are usually accepted also.



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## Savings will Vary Depending on Your Personal Situation

Your actual savings will vary depending on the following factors:

1. Other income that you may have.
2. Your marital situation.
3. The income from your spouse.

**Therefore, it is advisable to get competent professional advice before electing S-Corporation status for your business.**



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## Real Life SCORE Client – Consultant

In 2024, business owner elected S-Corporation status for her LLC. The business had profits of \$180,000 in 2024.

Had she not elected S-Corporation status for her LLC, her Federal taxes would have been as follows:

◦ Self-employment tax	\$19,853
◦ Federal income tax	49,436
◦ <b>Total Federal Taxes</b>	<b>\$69,289</b>



Thanks to electing S-Corporation status for her business, her Federal taxes were:

◦ Social Security, Medicare & other Federal tax	\$11,130
◦ Federal income tax	51,990
◦ <b>Total Federal Taxes</b>	<b>\$63,120</b>

**Total reduction in 2024 taxes \$6,169**

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## Workshop Agenda

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|---|---|
| <ol style="list-style-type: none"> <li>1. Federal Taxes and Taxing Regimes</li> <li>2. <b>Minimizing Federal Taxes</b> <ol style="list-style-type: none"> <li>a) S-Corporation Election</li> <li><b>b) Business Use of Home Deduction</b></li> <li>c) Business Use of Personal Vehicle</li> <li>d) Saving for Retirement</li> <li>e) Saving for Health Costs</li> </ol> </li> </ol> | <ol style="list-style-type: none"> <li>f) Saving for School and University Tuition</li> <li>g) Purchases of Equipment</li> <li>h) Maximizing Deductions</li> <li>i) Tax Credits for Businesses</li> <li>j) Cash vs. Accrual Accounting</li> <li>3. Concluding Comments</li> </ol> |
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## Business Use of Home Deduction

The IRS allows a deduction against a business's taxable income of the direct costs and the pro-rata costs allocated to the space in an owner's home that is used "**exclusively and regularly**" for business purposes.

The space can be a room, part of a room, a closet, a part of the basement or garage, or a separate building on the home's lot.

Contrary to popular belief, taking this deduction is **NOT** a red flag for an IRS audit.



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## Example Calculation of Deduction for Home Renter

Home expenses:		
Rent		\$24,000
Utilities		\$ 2,000
Repairs and maintenance		\$ 1,000
Insurance		\$ 500
Total		\$27,500
Space used for business	200 sq. ft.	
Total net space in home	1,500 sq. ft.	× 13.33%
<b>Total deduction for business use of home</b>		<b>\$ 3,667</b>

Note: Deduction is limited to the amount of taxable income of the business.



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## Example Calculation of Deduction for Home Owner

Home expenses:		
Mortgage interest		\$20,000
Depreciation		\$15,000
Real estate taxes		\$ 6,000
Utilities		\$ 2,000
Repairs and maintenance		\$ 3,000
Insurance		\$ 500
Total		\$46,500
Space used for business	200 sq. ft.	
Total net space in home	1,500 sq. ft.	× 13.33%
<b>Total deduction for business use of home</b>		<b>\$ 6,184</b>

Note: Deduction is limited to the amount of taxable income of the business.



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## Defining “Net Space of Home”

“Net Space of Home” means the total square footage of the home, less:

- ➔ Unlivable space (e.g., garage, unfinished basement)
- ➔ Common space (only hallways, bathrooms, utility rooms)

Using “Net Space of Home” to calculate your deduction will generate a **larger tax deduction for you!!!**

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## Renter Calculation – Excel Template

Name \_\_\_\_\_  
 Calculation of Business Use of Home Deduction  
 Saturday, January 21, 2023

The yellow colored cells require amounts to be entered into them in order to calculate the Deduction.

	Example	2022	2023	2024
Rent	\$ 28,200	\$ -	\$ -	\$ -
Utilities (electricity, gas, water, garbage)	\$ 2,900	\$ -	\$ -	\$ -
Repairs & Maintenance	\$ 50	\$ -	\$ -	\$ -
Renters Insurance	\$ 150	\$ -	\$ -	\$ -
Total home expenses	\$ 33,300	\$ -	\$ -	\$ -
Ratio of business space to total net space of home	13.22%	#DIV/0!	#DIV/0!	#DIV/0!
Deduction for Business Use of the Home	\$ 4,614	#DIV/0!	#DIV/0!	#DIV/0!
Total business space of the home in Sq. Ft.	200	0	0	0
Calculation of Net Space of the Home:				
Total space of the home in Sq. Ft.	2044	0	0	0
Less:				
Bathrooms (space in Sq. Ft.)	250	0	0	0
Hallways (space in Sq. Ft.)	225	0	0	0
Utility room (space in Sq. Ft.)	25	0	0	0
Net Space of the Home	1513	0	0	0

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## Homeowner Calculation – Excel Template

Name \_\_\_\_\_  
 Calculation of Business Use of Home Deduction  
 Saturday, January 21, 2023

The yellow colored cells require amounts to be entered into them in order to calculate the Deduction.

	Example	2022	2023	2024
Mortgage interest	\$ 28,200	\$ -	\$ -	\$ -
Real Estate Taxes	\$ 4,000	\$ -	\$ -	\$ -
Utilities	\$ 2,900	\$ -	\$ -	\$ -
Repairs & Maintenance	\$ 50	\$ -	\$ -	\$ -
Depreciation (depreciation, gas, water, garbage)	\$ 1,400	\$ -	\$ -	\$ -
Depreciation (depreciation)	\$ 4,000	\$ -	\$ -	\$ -
Depreciation (depreciation)	\$ 2,000	\$ -	\$ -	\$ -
Total home expenses	\$ 38,500	\$ -	\$ -	\$ -
Ratio of business space to total net space of home	13.22%	#DIV/0!	#DIV/0!	#DIV/0!
Deduction for Business Use of the Home	\$ 5,088	#DIV/0!	#DIV/0!	#DIV/0!
Total business space of the home in Sq. Ft.	200	0	0	0
Calculation of Net Space of the Home:				
Total space of the home in Sq. Ft.	2044	0	0	0
Less:				
Bathrooms (space in Sq. Ft.)	250	0	0	0
Hallways (space in Sq. Ft.)	225	0	0	0
Utility room (space in Sq. Ft.)	25	0	0	0
Net Space of the Home	1513	0	0	0
Depreciation of the building	\$ 700,000	\$ -	\$ -	\$ -
Depreciation cost of the building, including soil	\$ 480,000	\$ -	\$ -	\$ -
Less: Real estate taxes	\$ 40,000	\$ -	\$ -	\$ -
Adjusted cost (2017)	\$ 700,000	\$ -	\$ -	\$ -
Adjusted cost (2017)	\$ 700,000	\$ -	\$ -	\$ -
Total Depreciable Cost of the Building	\$ 700,000	\$ -	\$ -	\$ -
Depreciation	\$ 3,000	\$ 3,000	\$ 3,000	\$ 3,000



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## Claiming the Deduction as a Sole Proprietorship

Need to claim deduction on Form 8829. 

Instead of using Form 8829, you can use the simplified method for calculation the deduction, which is:  
 "square feet of space in home used exclusively for business" X \$5



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## How to Claim the Deduction for Partnerships and S-Corporations

For a partnership and an S-Corporation, the deduction is claimed by making the calculation as shown on the previous slides and **reimbursing the owner(s)**. The amount of the reimbursement is then claimed on

Form 1120S: Under "Other Deductions" (Line 19)  
 Form 1065: Under "Other Deductions" (Line 20)



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## Real Life SCORE Client – Custom Jewelry Manufacture and Sales Business

Business owner performs all the manufacturing of jewelry in her apartment. The business use of her home is 76%. The business had profits of about \$80,000 in 2019.

Had she not taken the business use of home deduction:	
◦ Federal Income Taxes	<b>\$9,936</b>
After taking the business use of home deduction:	
◦ Federal Income Taxes	<b>\$7,177</b>
<b>Total reduction in 2019 taxes</b>	<b><u>\$2,759</u></b>



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## Summary of Business Use of the Home Deduction

The deduction for business use of the business owner's home is a great way to create Federal income tax **savings** with no additional cost to the business or the business owner.



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## Workshop Agenda

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|---|---|
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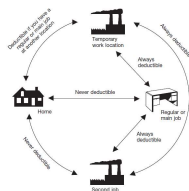
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## Business Use of Personal Vehicle Deduction

The IRS allows a deduction against a business's taxable income of business use of the owner's personal vehicle.

"Business use" is defined as all mileage that pertains to the business that is not "commuting".

**If you take a deduction for "business use of the home," you never have any commuting mileage as your home is your principal place of business.**



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### Business Use of Personal Vehicle Deduction Calculation Methods

IRS Rate per mile Method:		Actual Cost Method:	
Business miles driven	5,000	Gasoline and oil	\$2,000
IRS rate per mile 2025	× \$0.70	Repairs and maintenance	800
<b>Deduction</b>	<b>\$3,500</b>	Licenses fees and tags	300
		Car insurance	1,400
		Depreciation (\$30,000 cost)	6,000
		<b>Total actual costs</b>	<b>\$10,500</b>

Compare the Results:	
IRS Rate per mile Method	\$3,500
Actual Cost Method	\$4,375
<b>Deduction – Larger of the Two:</b>	<b>\$4,375</b>

Business miles driven:	5,000	=	X 41.67%
Total miles driven:	12,000		
<b>Deduction</b>			<b>\$4,375</b>

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### How to Claim the Deduction

The deduction is claimed on the following IRS forms and schedules:

- Sole Proprietorship:** On Schedule C, under "Car and Truck Expense"
- S-Corporation:** On Form 1120S, under "Other Deductions" (Line 19)
- Partnership:** On Form 1065, under "Other Deductions" (Line 20)

The deduction can be claimed whether or not the owner is reimbursed for the amount of the mileage deduction.



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### Summary of Business Use of Personal Vehicle Deduction

The deduction for business use of the business owner's vehicle is a great way to create Federal income tax **savings**.

However, to sustain such deduction upon IRS audit, documentation of business miles driven is paramount.



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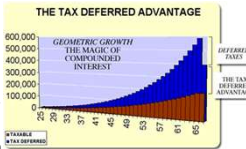
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## Benefits of Saving for Retirement

The benefit of saving for retirement within one of the IRS's tax-qualified plans is two-fold:

- Provides retirement income.
- Reduces either the owner's taxable income or the business's taxable income (or both) and **defers** Federal income taxes from the current year into retirement years when normally income is less.



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## Tax Qualified Retirement Savings Plans for Business Owners

Although there are other tax-qualified retirement plans, we will focus on the following seven plans:

- 1 – One Participant 401(k) Plan
- 2 – SEP Plan
- 3 – Safe Harbor 401(k) Plan
- 4 – SIMPLE IRA Plan
- 5 – Traditional IRA Plan
- 6 – Roth IRA Plan



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## One Participant 401(k) Plan, Individual 401(k) Plan or Solo 401(k) Plan

Under a Solo 401(k), the owner of a business can make elective deferrals of salary up to \$23,500 per year (\$31,000 if 50 years of age or older)(\$34,750 if 60 to 63 years of age).

In addition, a business can make tax deductible contributions to the owner's account up to 25% of the employee's compensation.

Solo 401(k) plans are the best retirement savings plan for a business owner with no employees. However, the plan needs to be set up well before the end of the year and may require administrative fees.



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## Real Life SCORE Client – Logistics Consultant

Business owner is a logistics consultant and had profits from his business of \$162,700 in 2024. In 2024, he established a Solo 401(k) Plan for himself. In 2024, he had salary deferrals of \$23,000 contributed to the plan and his business contributed \$25,000 to the Plan (25% of his gross wages of \$100,000).

Had he not contributed to a Solo 401(k) Plan:

• Federal Income Taxes **\$67,396**

After having made the contributions to the Plan:

• Federal Income Taxes **\$45,074**

**Total reduction in 2024 taxes \$22,322**



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## Simplified Employee Pension Plan, or SEP Plan

Under a SEP Plan, a business can make tax deductible contributions to an owner's (and employee's) SEP-IRA which cannot exceed the lesser of:

- 25% of the employee's compensation (or about 20% of taxable income if the business is a sole proprietorship);
- The business's taxable income; or,
- \$68,000 (\$75,500 if 50 years of age or older)

Very good retirement plan for a business owner with no employees. A SEP Plan is easy to set up, can be created and funded as late as 15 October of the subsequent year and often requires no administrative fees.



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## Real Life SCORE Client – Attorney in Sole Practice

Business owner is an attorney who supports school districts in lawsuits. She established a SEP Plan for himself many years ago. In 2021, her business made a \$15,000 contribution to the SEP Plan on her behalf (25% of her gross wages of \$60,000).

Had her business not contributed to the SEP Plan:  
 - Federal Income Taxes **\$15,658**

After having made the contributions to the SEP Plan:  
 - Federal Income Taxes **\$12,912**

**Total reduction in 2021 taxes \$2,746**



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## Safe Harbor 401(k) Plan

Under a Safe Harbor 401(k) Plan, all eligible employees of a business can make elective deferrals of salary up to \$23,500 per year (\$31,000 if 50 years of age or older), or 100% of their compensation, whichever is smaller.

The business must 100% match its employees' 401(k) contributions up to 3% of their compensation and 50% of employees' contributions between 3% and 5% of their compensation.

Safe Harbor 401(k) Plans are the best choice for a small business with employees in which the owner desires to save a lot for retirement. There are generally administrative fees associated with the Plan. Lastly, the Plan is not subject to annual discrimination testing of a traditional 401(k) Plan.

### Safe Harbor 401(k) Plans



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## Employer Matching – How It Works

This table describes how the Safe Harbor 401(k) Plan required employer matching works.

The left column shows the employee's contribution to the Safe Harbor 401(k) Plan.

The right column shows the required employer matching contribution to the Safe Harbor 401(k) Plan.

Percentage W-2 Income (Amount of deferral)	1. Basic Matching
0% (\$0)	0% (\$0)
1% (\$1,500)	100% match Total: 1% = \$1,500
2% (\$3,000)	100% match Total: 2% OR \$3,000
3% (\$4,500)	100% match Total: 3% OR \$4,500
4% (\$6,000)	100% up to 3%, 50% of the next 1% match Total: 3.5% OR \$5,250
5% (\$7,500)	100% up to 3%, 50% of the next 2% match Total: 4% OR \$6,000
6% (\$9,000)	No additional contribution required

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### Real Life SCORE Client – Owner of Cat Café

Business owner established a Safe Harbor 401(k) Plan for herself and her employees in 2019. In 2019, she contributed \$19,000 contribution to the Plan and the business made a matching contribution of \$2,000 on her behalf (4% of her gross wages of \$50,000).

Had the business and she not contributed to the Plan:


- Federal Income Taxes **\$24,446**

After having made the contributions to the Plan:

- Federal Income Taxes **\$19,982**

**Total reduction in 2019 taxes \$4,464**

Cost to the business for the Plan \$2,414



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### SIMPLE IRA Plan

Under a SIMPLE IRA Plan, a business's employees can make tax-deductible contributions that reduce their compensation up to \$16,500 annually (or \$20,000 if 50 years of age or older and \$21,750 if between 60 and 63 years of age). The employer must either:

- Match dollar-for-dollar employee contribution up to 3% of their compensation, or
- Contribute 2% of compensation for all employees, whether they contribute or not.

As a result, SIMPLE IRA Plans are ideal for a business with employees with a business owner who desires to minimize the cost of the plan as there are generally no administration fees.



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### Real Life SCORE Client – Owner of Physical Therapy Clinic

Business owner established a SIMPLE IRA Plan for herself and her one employee in 2018. In 2021, she contributed \$16,000 contribution to the Plan (she is over 50 years of age) and the business made a matching contribution of \$1,500 on her behalf (3% of her gross wages of \$50,000).

Had the business and she not contributed to the Plan:


- Federal Income Taxes **\$17,809**

After having made the contributions to the Plan:

- Federal Income Taxes **\$14,208**

**Total reduction in 2021 taxes \$3,601**

Cost to the business for the Plan \$1,285



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## Traditional IRA Plan

Under a Traditional IRA Plan, a business's owner can make elective contributions that reduces her/his taxable income up to \$7,000 (\$8,000 if owner is age 50 or older) annually.

There is no "phase-out" of the amount of the contribution if the business owner and spouse are not covered by a retirement plan.

However, if one or both are covered by a retirement plan, then there's an income limitation (\$165,000 if unmarried, \$246,000 if married filing jointly).

Traditional IRA Plans are ideal for a business owner who has employees but does not want to manage an employer sponsored retirement plan yet desires to save for retirement.



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## Spousal IRA Plan

If the spouse of the business owner has no income, that spouse may be eligible to contribute to a Spousal IRA.

Under a Spousal IRA Plan, the spouse can make elective contributions that reduces their taxable income up to \$7,000 (\$8,000 if spouse is age 50 or older) annually.

However, if the business owner is covered by a retirement plan, then there's an income limitation of \$246,000.

Spousal IRA Plans are ideal for a married couple when the business owner makes contributions to an IRA and the couple want to maximize their retirement savings.



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## Roth IRA Plan

Generally, you can contribute to a Roth IRA if you have earned income from wages or self-employment and your modified AGI is less than:

- \$246,000 for married filing jointly; or,
- \$165,000 for single, head of household, or married filing separately and you didn't live with your spouse at any time during the year.

Under a Roth IRA Plan, a business's owner and spouse can make elective contributions up to \$7,000 each (\$8,000 if owner is age 50 or older) annually. **However, contributions are NOT tax deductible.**

Contributing to a Roth IRA is better than contributing to a Traditional IRA when the business owner's total taxable income is less than \$48,500 if unmarried or \$97,000 if married.



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## Making a Choice and Set-up

Ask an Advisor for assistance in choosing plan:

- CPA
- Your Friendly Banker or Stockbroker
- Joe Heinrich

Set-up can be done at:

- Financial institution (e.g., bank)
- Brokerage firm (e.g., Charles Schwab)
- Intermediary service (e.g., [www.guideline.com](http://www.guideline.com))



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## Objective for Saving for Health Care Costs

By using one of the tax-qualified health care savings plans, you can reduce your after-tax cost of out-of-pocket medical expenses and thus save Federal income taxes.

Such saving can reduce your out-of-pocket costs generally by 10% to 40%, depending on your highest marginal Federal income tax rate.



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## Health Savings Account - Requirements

### Requirements:

- 1) Be enrolled in a "high-deductible health plan" which needs to have a deductible as follows:
  - Self-only Coverage Deductible + Out of Pocket Range: At least \$1,650 but not more than \$8,300
  - Family Coverage Deductible + Out of Pocket Range: At least \$3,300 but not more than \$16,600
- 2) Need to be under age 65.
- 3) Need to have no other disqualifying medical insurance



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## Health Savings Account – Contributions and Benefits

You can annually contribute up to \$4,300 for yourself or \$8,550 for a family to be used for "qualified medical expenses". If 55 years of age or older, an additional \$1,000 can be contributed.

Can be established by an individual or by an employer.

**Amounts contributed are not subject to Federal income tax.**

Simple to set up, simple to make contributions, relatively simple to make payments for qualifying medical expenses.

### Four Tax Advantages of HSA's



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## Health Savings Account – Can Act Like an IRA During Retirement

Once you reach age 65, amounts can be withdrawn for either:

- a) Out-of-pocket medical costs during retirement
- b) Personal use (i.e., not medical related)

**Amounts withdrawn for personal use are subject to Federal income tax.**

### Tax Benefits of Health Savings Accounts (HSAs)



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## Other Health Savings Plans

### Flexible Spending Arrangement

An employer-sponsored plan in which you can save annually up to \$3,300 through salary reductions.

Requires amounts in account to be used by the end of the year, otherwise they are forfeited except for \$660 maximum rollover.

### Qualified Small Employer Health Reimbursement Arrangement

An employer-sponsored plan in which only the employer can make contributions, but contributions are not limited.

- Only employer can make contributions
- Must comply with Rev. Ruling 2017-67
- Good for providing a "medical stipend" to employees



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## Workshop Agenda

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  - g) Purchases of Equipment
  - h) Maximizing Deductions
  - i) Tax Credits for Businesses
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## Saving for Education Expenses

The IRS offers two plans for saving for education expenses of your children and grandchildren. They are:

- Qualified Tuition Program – or commonly known as "529 Plan"
- Coverdell Education Savings Account – limited to \$2,000 contribution per year, thus not very useful.



In addition, a Roth IRA may provide a funds for education purposes and may be more flexible.

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### Qualified Tuition Program – 529 Plan

Contributions to a "529 Plan" are limited to \$19,000 per year per beneficiary. **Contributions are not tax deductible.**

Amounts saved in a "529 Plan" can be used for K-12 education tuition to a private school, up to \$10,000 per child per year.

Amounts in the 529 Plan can also be used for college tuition, fees, books, supplies and equipment, computers, and room and board if the student is enrolled on at least a half-time basis.

Amounts withdrawn (including earnings) are not taxable. **Thus, the earnings on the funds will never be taxed.**



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### New Feature for 529 Plans

If money is left over in a 529 Plan after graduation, the beneficiary may contribute up to \$35,000 of the funds in the 529 Plan over a 15-year period to a Roth IRA.

Thanks to this new provision in the tax code, a graduate can get a jumpstart in saving for retirement.

At an annual growth rate of 7% on the initial \$35,000 over a 40-year period, that Roth IRA account will be worth \$560,000.



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### Using a Roth IRA for Education Costs

Roth IRAs can also be used to pay for qualified education expenses, which makes them quite versatile as either a retirement plan or an education savings plan, or both.

Pro: No need to name a beneficiary.

Con: Limited to \$7,000 contribution per year.



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## Using a Roth IRA for Education Costs - Example

Married couple with combined income of \$175,000 save \$500 per month for 18 years in a Roth IRA since the birth of their child.

After 18 years, they have saved \$108,000 in the Roth IRA plus, assuming growth of 6%, the total value of the Roth IRA is \$190,000.

The Roth IRA can be used either for education expenses for the child or a retirement fund for the parents, or both.



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## Workshop Agenda

- 1. Federal Taxes and Taxing Regimes
- 2. **Minimizing Federal Taxes**
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  - c) Business Use of Personal Vehicle
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  - e) Saving for Health Costs
- f) Saving for School and University Tuition
- g) **Purchases of Equipment**
  - h) Maximizing Deductions
  - i) Tax Credits for Businesses
  - j) Cash vs. Accrual Accounting
- 3. Concluding Comments

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## Benefit of Purchases of Equipment

The benefit of purchasing equipment and creating a depreciation deduction (or Sec. 179 expense) is to reduce the business's taxable income and save Federal taxes in the current year and near future years.

This strategy should only be used if the purchase of equipment is absolutely necessary AND should be timed to take advantage of the year in which the business has more taxable income.



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## 4 Ways to Get a Deduction for Purchases of Equipment

### 1. Equipment Purchases for Items Individually Less than \$2,500 Each:

All individual equipment of \$2,500 and less are deducted in their entirety in the year purchased.

The expense needs to be categorized as "Repairs & Maintenance" on the business's Federal income tax return to be deductible.

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## 4 Ways to Get a Deduction for Purchases of Equipment

### 2. Section 179 Expense:

For equipment purchases in excess of \$2,500, the ability to deduct all or any part of the cost of equipment purchased during the year, not to exceed a business's taxable income.

### 3. Bonus Depreciation:

For equipment purchases in excess of \$2,500, the ability to deduct most or part of the cost of qualifying equipment purchased during the year.

Year	Bonus depreciation
2023	80%
2024	60%
2025	40%
2026	20%
2027 and future years	0%

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## 4 Ways to Get a Deduction for Purchases of Equipment

### 4. Depreciation:

For purchases in excess of \$2,500, the ability to deduct the cost of the equipment ratably over an equipment's useful life starting in the year of purchase.

Example: Purchase of a car for \$20,000

- Year 1: \$4,000
- Year 2: \$6,400
- Year 3: \$3,840
- Year 4: \$2,304
- Year 5: \$2,304
- Year 6: \$1,152

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### Example of a "Smart" Equipment Purchase

It is December 2025. A machine needs to be replaced within the next 10 months. It will cost \$40,000. Owner's taxable income in 2025 will be \$130,000 and is forecasted to be \$100,000 in 2026. Should owner buy the machine in 2025 or 2026?



2025 – Why?:

Equipment needs to be replaced very soon.

Taxable income in 2025 will be greater than in 2026.

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### Example of a "Not-So-Smart" Equipment Purchase

It is December 2025. Business has a car that is two years old and in good working order. Owner wants to save taxes in 2025 so owner trades in old car for a new car and pays \$40,000. Owner's taxable income in 2025 will be \$100,000 (before car purchase) and will be at least \$130,000 in 2026.



Why is this **not** a "smart" equipment purchase?:

- Car does not need to be replaced very soon.

- Taxable income in 2026 will be greater than in 2025.

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## Deductible Food, Drink and Meal Expenses

Following are the types of expenses and their deductibility for Federal income tax purposes:

- Meals with customers and prospects at a restaurant: 50% deductible
- Food & beverages provided at an event (i.e., "Presentation Expenses"): 100% deductible
- Employee parties: 100% deductible
- Meals – all other: 50% deductible



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## Suggested Classifications of Meals/Food

To maximize the deductibility of meals and food, you should set up the following accounts in your accounting system (e.g., QuickBooks):

- Business meals at restaurants
- Meals – all other
- Employee parties
- Presentation expenses

You should have an account called "Entertainment expense" for nondeductible entertainment expenses such as tickets to events for customers, prospective customers and business associates.



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## Charitable Contributions

Charitable contributions are not deductible by the business. They are only deductible by the business owner if the business owner itemizes deductions on Schedule A of Form 1040.

Therefore, it is best to get something in return for the amounts your business gives to a charitable organization so your business can honestly classify the payments as one of the following:

- Sponsorship
- Marketing
- Advertising



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## Bunching of Charitable Deductions

If you give a lot to charitable organizations, consider "bunching" your contributions in a single year instead of spreading them out over many years.

By making charitable contributions of \$10,000, you may not be getting any tax benefit.

However, by using a "Donor Advised Fund", you can bunch several years of charitable contributions in a single year and reap some sizable tax savings.

The chart shows two scenarios over five years (2023-2027). In the 'NO BUNCHING' scenario, \$10,000 is donated each year, resulting in no tax savings. In the 'BUNCHING' scenario, \$50,000 is donated in 2023, with no donations in the other years, resulting in \$10,366 in tax savings. The y-axis represents tax savings from \$0 to \$60,000. The x-axis shows years 2023 through 2027. A legend indicates Standard Deduction (yellow), EIT (green), and Charitable (dark green).

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## Employing Your Minor Children

Employing your children in your business can provide some tax advantages.

Children under the age of 18 are not subject to Social Security, Medicare, or Federal Unemployment taxes if the parents' business is a sole proprietorship or a partnership.

A child who earns less than the standard deduction does not owe any federal income taxes. In 2025, that amounts to \$15,000 per child sheltered from Federal income taxes annually. The parent will still be able to claim the child as a dependent for the Child Tax Credit.

However, be aware of Washington state statutes regarding employing a minor.

-- You will receive an article about this opportunity. --

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## Workshop Agenda

1. Federal Taxes and Taxing Regimes
2. Minimizing Federal Taxes
  - a) S-Corporation Election
  - b) Business Use of Home Deduction
  - c) Business Use of Personal Vehicle
  - d) Saving for Retirement
  - e) Saving for Health Costs
- f) Saving for School and University Tuition
- g) Purchases of Equipment
- h) Maximizing Deductions
- i) Tax Credits for Businesses
- j) Cash vs. Accrual Accounting
3. Concluding Comments

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## Tax Credits for Businesses

1. Retirement Plans Startup Costs Credit

2. Credit on employer Social Security tax paid on employees' tips in restaurant, cafes and drinking establishments

3. Research & Development Credit



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## Retirement Plans Startup Costs Credit

Small businesses may be able to claim a tax credit of up to \$5,000 per year, for three years, for the costs of starting and administering a SEP, SIMPLE IRA or 401(k) plan.

The amount of the credit is 50% of the costs incurred. The credit amount is the greater of \$500, or \$250 multiplied by the number of employees (excluding the owner of the business). An "auto-enrollment" feature to the retirement plan can add another \$500 tax credit.

In addition, there's a credit of up to \$1,000 per employee for if the business matches the employee's retirement plan contributions.

**In summary, these credits could offset the entire cost of sponsoring a retirement plan during the first 2 years.**



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## Credit on Employer Social Security Tax Paid on Restaurant Employees' Tips

Owners of restaurants, bars, cafes and other eating and drinking establishments can claim a tax credit on their personal Federal tax returns for the employer Social Security and Medicare Taxes paid on employee tips.

Tax credit is 7.65% of the amount of employee tips reported on the Form W-2 of the employees.

To claim the tax credit, Form 8846 needs to be attached to the business owner's Form 1040.

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## Increasing Research Expense Credit

Research activity needs to meet the four-part test as shown to the right.

Qualifying R&D expenses need to be wages, supplies, contract research and computer leasing costs.

Documentation of the activities is very important to substantiate the credit.

Tax credit is 20% of the incremental R&D expenses over the base year.



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## Cash versus Accrual Accounting Methods

### Objective:

The objective of electing an accounting method is to choose the one that will reduce your Federal taxable income and/or Washington taxable sales to defer paying Federal income and self employment taxes and Washington Business & Occupation taxes for generally one year.

**Put the  
POWER OF  
TAX DEFERRAL  
to work for you**

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## There are Two Types of Accounting Methods

**Cash Basis of Accounting:** A transaction is recorded only when cash is paid or received.

**Examples:**

- No sale is recorded until cash is received.
- No expense is recorded until the payment is made.

**Accrual Basis of Accounting:** A transaction is recorded as it occurs.

**Examples:**

- Sales are recorded when the goods or services are delivered and invoiced to the customer.
- Expenses are recorded when they are incurred and a liability is created.

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## When and How to Choose

**When to choose:**

A business elects its accounting method in its first year of business.

**How to choose:**

A business elects its accounting method on its Federal income tax return in its first year of business.

Changes from one method to another can be made after the initial election, but will require filing Form 3115 with the IRS and asking permission to change.



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## Which Accounting Method will Defer Business Taxes?

In general, the **Cash Method** is more advantageous from a Federal income tax standpoint and simpler to operate.

**However:**

If your customers pay you for your products or services immediately; and if you tend to pay your purchases on credit.

(or)

If you receive substantial prepayments from customers prior to delivering the products or services,

Then, **consider the Accrual Method.**

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## Real Life SCORE Client – Owners of a Veterinary Hospital

Business owners chose the accrual method of accounting in 2016, their first year in business. As of the end of 2019, the business was able to deduct **\$73,081** more in expenses than if the business had been using the cash method.

**Thus, the business owners were able to defer about \$14,032 in Federal income taxes.**



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## Document Retention - What to Keep?

All invoices and receipts supporting business expenses and deductions.

All invoicing to customers and customer payment records.

All accounting / bookkeeping information.

All Federal, state and local tax returns and reporting.

All other records that support information provided to taxing authorities.



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## Document Retention - How to Keep?

### Format:

- Electronic – be sure to do regular back-ups
- Paper – be sure to protect from hazards

### Manner of Filing:

- By month (preferred)
- By supplier and customer

If you use QuickBooks Online, you can attach your electronic documents to the transaction in the system.



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## Document Retention - How Long to Keep?

### Supporting documents:

7 years from the date the related Federal income tax return is filed.

### Federal income tax returns:

Indefinitely



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## Should You Get an Extension for Your Federal Tax Return?

**YES !!**

Why???

- Allows you to work with your tax professional after her/his busy season.
- It is not a "red flag" that increases your IRS audit risk.

However, ensure your taxes are fully paid by the original due date of your tax return !!!

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### Federal Income Tax Return

It is better to have a competent professional review your tax return than prepare your return, if you feel relatively good about preparing your own tax return.

A competent professional can focus on opportunities when she/he reviews a tax return, making the owner look like this:



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### Federal Income Tax Return

If you have a competent professional prepare your tax return, review it very, very carefully for completeness and correctness.

Not reviewing your tax return looks like this:



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### Rules of the Road for Your Taxes

1. Use all legal means to save and defer taxes.
2. When in doubt, seek competent advice.
3. Put aside cash for paying taxes. (i.e., Pay the governments before paying yourself.)
4. Pay all taxes when due and be sure to be fully paid up by the due date of the return. (i.e., Don't use the IRS or WA Dept. of Revenue as a lender.)



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### Before Leaving Here Today . . .

- 1. **Complete the online evaluation** with your very frank comments.
- 2. **Send me an email**, if you'd like to get my advice or counseling in the future.
- 3. Resolve to **implement at least one tax saving or deferral strategy** that you learned here today.



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### Sponsored by GDM Private Financial Solutions



GDM Private Financial Solutions is a highly skilled Bellevue, WA CPA firm offering innovative accounting services and tax planning solutions for small business owners. Our mission is to remove financial obstacles and skillfully manage your tax obligations to improve your business and your bottom line.

At GDM Private Financial Solutions, we understand the difficulties behind choosing the right CPA for you or your business, which is why we offer a **free initial consultation**. This allows you to get to know us and us to get to know your business - so we can build a long-term professional relationship.

Give us a call today at **425-283-5425** to schedule your **free initial consultation**.

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### THANK YOU FOR YOUR PARTICIPATION



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