Beyond the Numbers

FINEMAN WEST & COMPANY

November 2016 Newsletter

Dear Clients and Friends,
In this issue of our newsletter we discuss how S Corporation business owners can balance their salary and dividend amounts to avoid heavy payroll taxes. Also featured in this issue, what the self-employed need to know about employment taxes. For more information about featured stories in this newsletter, please contact the team at Fineman West & Company.

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Balancing Salary and Dividend Amounts for S Corporation Owners

For business owners of an S Corporation, the company probably pays owners a salary that exhibits the work accomplished for the company and in turn said owners must pay payroll taxes on some or all of earned income. However, S Corporations and their owners can avoid payroll taxes by dividing profits in the form of dividends rather than salary. Medicare tax on wages results in an additional 0.9% on wages in excess of $200,000 ($250,000 for joint filers and $125,000 married but filing separately), which has a greater potential tax savings from classifying payments as dividends.

To avoid penalties and interest from IRS auditing due to unreasonably low and unpaid payroll taxes, S Corporations should document reasonable salaries for each position using compensation surveys, comparable industry studies and company financial data. Furthermore, owners should have compensation amount reasons documented in corporate minutes and reviewed by a tax profession before being finalized.

To prove reasonable salary amounts, these factors should be considered:

7. Training and experience
8. Duties and responsibilities
9. Time and effort devoted to business
10. Dividend history
11. Payments to non-owner employees
12. Timing and manner of paying bonuses to key people
13. Compensation agreements

For more information regarding the information provided or for help determining salary and dividends to keep tax liability low for your company, please contact one of our tax professionals. Contact Our Team

Contact Us

What The Self-Employed Need To Know About Employment Taxes

In addition to income tax, you must pay Social Security and Medicare taxes on earned income, such as salary and self-employment income. The 12.4% Social Security tax applies only up to the Social Security wage base of $118,500 for 2016. All earned income is subject to the 2.9% Medicare tax. The taxes are split equally between the employee and the employer. But if you're self-employed, you pay both the employee and employer portions of these taxes on your self-employment income. Another employment tax that higher-income taxpayers must be aware of is the additional 0.9% Medicare tax. It applies to FICA wages and net self-employment income exceeding $200,000 per year ($250,000 for married filing jointly and $125,000 for married filing separately).

If your wages or self-employment income varies significantly from year to year or you're close to the threshold for triggering the additional Medicare tax, then income timing strategies may help you avoid or minimize it. These strategies include withholding rules:

1. Employers must withhold the additional Medicare tax beginning in the pay period when wages exceed $200,000 for the calendar year - without regard to an employee's filing status or income from other sources.
2. Your employer might not withhold the tax even though you are liable for it due to your self-employment income.
3. Consider filing a W-4 form to request additional income tax withholding, which can be used to cover the shortfall and avoid interest and penalties.
4. Make estimated tax payments if you do owe the tax but your employer isn't withholding it.

Deductions for the self-employed, the employer portion of employment taxes (6.2% for Social Security tax and 1.45% for Medicare tax) is deductible above the line. (No portion of the additional Medicare tax is deductible, because there's no employer portion of that tax).

As a self-employed taxpayer, you may benefit from other above-the-line deductions as well:

1. You can deduct 100% of health insurance costs for yourself, your spouse and your dependents, up to your net self-employment income.
2. You also can deduct contributions to a retirement plan and, if you're eligible, an HSA for yourself.
3. Above-the-line deductions are particularly valuable because they reduce your adjusted gross income (AGI) and modified AGI (MAGI), which are the triggers for certain additional taxes and the phase-out of many tax breaks.

For more information on the ins and outs of employment taxes and tax breaks for the self-employed, please Contact Our Team.

Contact Us

Fineman West & Company Celebrating Halloween!

Fineman West & Company's team members Harold West, Parnia Padkhou and Cindie Banh paid a visit to a client on Halloween and had the pleasure of conducting business with Pokemon characters. Happy Halloween from Fineman West & Company!

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