

**TAX TALK**  
**BY JEFFREY D. SKOLNICK, CPA, M.S. TAXATION**

**ADVANTAGES OF EMPLOYING FAMILY MEMBERS**

In today's environment there are many businesses that are owned as sole proprietorships, partnerships and LLCs. If you are an owner of any of these types of entities, then you may benefit from employing your minor child.

**How does employing my child benefit my business?**

There is a provision in the tax code which exempts wages paid to a minor child from being taxed for social security or federal unemployment purposes. New Jersey has a similar rule that exempts the wages of minor children from state unemployment taxes.

In order to be eligible for the exemption the employer must be either a sole proprietorship, single member LLC, partnership or LLC with the only partners/members being the child's parents. C corporations, S corporations and partnerships and LLCs with partners and/or members other than the child's parent are ineligible for the exemption.

The exemption applies to parents and spouses of the employer for only federal and state unemployment tax purposes. There is no exemption from social security and Medicare taxes for any relatives other than minor children. Based on these facts the remainder of this article will focus on hiring children only.

**Are there any other advantages besides saving payroll taxes?**

Yes, a child has a standard deduction that is the greater of \$950 or his/her earned income plus \$300 (but no greater than \$5,800 in 2011). This means you can pay your child as much as \$5,800 as an example which would lower your taxable income and at the same time is exempt from tax on the child's return.

**How much benefit would I actually see?**

If you are a qualifying entity (as listed above) and you're in the 25% tax bracket and you pay your minor child \$5,000 you would save \$1,250 ( $\$5,000 \times 25\%$ ) plus self employment tax of \$665 ( $\$5,000 \times 13.3\%$ ). That is a total tax savings of \$1,915. This figure of over \$1,900 does not include any state benefits which may be another few hundred dollars.

**Is there a catch?**

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The only catch is that the services performed by your child must be necessary and reasonable. Reasonable services a minor child may perform could include filing, photocopying, emptying the trash, cleaning and some computer work.

If you try to pay your child \$25 an hour to photocopy and empty the trash, then that would not be considered reasonable. If, however, your child worked 10 hours a week and was paid \$10 an hour that may be considered reasonable.

**Conclusion**

This article explains some basic concepts regarding employing your child. You would be well advised to speak to a professional before implementing any strategies or you may find unintended consequences such as student eligibility for financial aid being reduced down the road.