**5 Tax Reduction Strategies**

American Society for Asset Protection

Americans pay more in taxes each year than they spend on food, clothing, and housing combined, so reducing your taxes to the legal minimum can greatly increase your ability to build wealth. Judge Learned Hand said, “Anyone may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the treasury; there is not even a patriotic duty to increase one’s taxes.” Supreme Court Justice Sutherland declared, “The legal right of a taxpayer to decrease his taxes or to altogether avoid them by means which the law permits cannot be doubted.” Here are five strategies to reduce your taxes to the legal minimum.

**Strategy #1 - Create Non-Taxable Income**

The IRS allows you to rent out your home for up to fourteen days each year without having to declare the rent as income. When a business partner or client comes into town and stays at your home, you can charge your corporation rent for the room. You can also have a company party or trainings at your home and rent your home to your corporation for the day. The corporation deducts the rental expense, and you enjoy the rental income tax free.

**Strategy #2 - Spread Income**

If you are in a federal tax bracket higher than 15%, you may be able to reduce your taxes by setting up a Nevada C corporation and have up to $50,000 of your income flow to this corporation. Nevada has no state income tax and has a federal tax rate of 15% on the first $50,000 of taxable income. Your corporation can retain these earnings so you are not double taxed. If you had a personal marginal federal income tax rate of 28% and a state income tax rate of 7%, you would pay $17,500 in federal and state income tax on this $50,000. If, however, this $50,000 flowed to a Nevada C corporation, you may only pay the federal corporate tax rate of 15% (depending on the activity of the corporation), or $7,500, saving you $10,000 in taxes.

Another application of this strategy is to spread income to children in lower tax brackets. Instead of paying your children’s expenses directly with after-tax dollars, hire your children and pay them for the work they do and have your children pay for their own clothes, food, school, etc. from the money they earn. You can deduct the wages as a business expense, and your children will pay taxes at their lower tax bracket.

**Strategy #3 - Maximize Deductions**

There are thousands of items that are allowed as business expenses. You want to make sure as many expenses as possible are deducted as business expenses. Expenses you may not be taking full advantage of as a business deduction are your medical expenses. Within a sole proprietorship or an S corporation, there is a limit on the medical expenses you can deduct. With the right provisions in a C corporation, you can deduct all medical insurance premiums and all out-of-pocket medical expenses for co-pays, medications, first aid items, etc.

**Strategy #4 - Defer Income**

One way the IRS allows you to defer income is by contributing to a retirement plan. A retirement plan that works well for a business with no employees (you may have another business with employees) is a Simplified Employee Pension Individual Retirement Account (SEP IRA). The IRS allows you to contribute 18.58% of net profit (maximum of $50,000 per year) to your SEP IRA for retirement. If you have $100,000 net profit in your business, you would be able to contribute up to 18.587%, or $18,587, to your retirement account. You would get to deduct the contribution, saving you thousands in federal and state taxes. Thus, money goes into your SEP IRA tax-free and grows tax-free. SEP IRA funds are taxed at ordinary income tax rates when qualified withdrawals are taken after 59.5 years of age.

**Strategy #5 - Proper Use of Entities**

The tax rules are different for S corporations, C corporations and Sole Proprietorships. You want to use the entity or entities which require you to pay the least amount of tax. For example, if you operate your business as a sole proprietor, all profit (up to the taxable maximum) is subject to Social Security and Medicare taxes. In an S corporation, profits are distributed through a K-1 and are not subject to Social Security and Medicare taxes. Having your profits flow to you as K-1 income, instead of as profit from a sole proprietorship, could save you thousands each year in Social Security and Medicare taxes.

For example, if a sole proprietorship has a profit of $100,000, a 15.3% tax (12.4% Social Security tax and 2.9% Medicare tax) would have to be paid on the entire $100,000, totaling $15,300 ($100,000 x 15.3%). In comparison, if an S corporation has a profit of $100,000 and you pay yourself a reasonable salary of $40,000, the other $60,000 would flow to you as profit (K-1) and is not subject to Social Security and Medicare taxes. You only pay social security and Medicare tax on the $40,000 salary, for a tax of $6,120 ($40,000 x 15.3%). In this scenario, using an S corporation would save $9,180 ($15,300 - $6,120) in taxes each year. While it would be nice to have the whole $100,000 excluded from Social Security and Medicare tax, the IRS requires that owner-employees of an S corporation be paid a salary that is a “reasonable amount” for the work being performed.

**Conclusion**

As a result of people not using all the deductions and laws available, billions of dollars are overpaid in taxes. According to the IRS commissioner, millions of taxpayers are overpaying their taxes each year. Begin using these five strategies to avoid paying more than you are required in taxes.