

Make College Savings - and Your Kids - Work for You

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There seems to be an abundance of plans available today to pay for your child's college costs: pre-paid tuition and 529 are just a couple of them. The problem is that you must pump in your money in order to make these plans work! But there are alternatives. One idea is to put your kids on your payroll.

You say your kids are already on your payroll, but are they just getting into your pockets and your wallet? Are your funds getting tapped on a regular basis? Want to make that "legal and deductible?" You can put your kids on the payroll and fully deduct what you pay them in salary, and if you structure it properly, they pay no taxes on the money they receive. In 2006, you could pay your child up to \$4,700 without any tax liability for them. What does that do for you? Let's assume that you are in a 30 percent tax bracket with both federal and state taxes. If you write your child a check for \$4,700, at your tax rate (30 percent), that only costs you \$3,290. If you file at a combined rate of 40 percent, it only costs you \$2,820.

Right now, for you to give your kids \$4,700, it would cost you \$6,715. You start with that amount and then have to pay taxes to get to the net amount of \$4,700. At a 40 percent tax rate, you start with \$7,833. So, if you are in a 30 percent combined tax rate, which would you rather spend to give your child \$4,700: \$2,820 or \$6,715? I'll bet it didn't take you any time at all to come to a decision! At a 40 percent rate, the difference is \$5,013. That's a lot of money. Each year, the amount you can pay your child with no income tax liability to them will increase.

Here are some more details on how this works. If you are not incorporated, wages paid to a child under age 18 are not subject to Social Security or Medicare taxes. Children under the age of 15 are limited to working three hours per day, 18 hours per week during the school year. During the summer, they can work a full 40-hour week. You must file the I-9 form and complete a W-4 Form on them, and write "exempt" on line #7 of the W-4 form. I would suggest you keep a time card so you can show the number of hours worked.

What, you might ask, can a child do in your office? How about change the paper rolls on the headrest, empty trash cans, and help with computer problems. How about licking and stuffing envelopes, and stamping them, too! Get creative, but make sure that they are really working.

I would not suggest that you put your 3-year-old on the payroll quite yet! That may not hold up if you are ever audited. I also suggest that you not pay your child more per hour than what you are paying the CA who has been with you for 20 years! That tends to raise a red flag, too. I would not put a child on the payroll until they are at least 8 years old. You can do it at an earlier age if you use them in any advertising or promotion.

Want to pay them more? You can. Pay your kids an additional \$4,000 and let them set up their own IRA. This is the "regular" IRA, not the Roth IRA. With the regular IRA, the contribution is paid with "before tax" dollars. Now you can pay them \$8,700 and get a full deduction as a business expense, and they pay no taxes on that money. When they are ready for college, they can cash in their IRA

and pay taxes and a penalty, but it will still be lower than your rate. Uncle Sam will still be paying almost 40 percent of their total college expenses.

If you are going to do this, here are some things to keep in mind so you don't run into any problems with the IRS:

1. Keep pay within reason.
2. Complete I-9 and W-4 forms. On line #7 of W-4, write "exempt."
3. For the first 90 days, pay them a training wage at the minimum wage level.
4. Kids under age 15 can work only three hours per day during school year. During summer, they can work 40 hours per week.
5. Pay them an additional \$4,000 for work done so they can fund their own Regular IRA.
6. Make sure they are performing a legitimate job. Don't give the IRS a reason to get angry.

You also can "lease" your equipment from your kids. Take all of your equipment that has fully depreciated and "gift" it to a trust. The trust then leases the equipment back to you. Your lease payment to the trust is tax deductible as a business expense. The trust can split the money among your kids before the end of the year, so the trust will pay no taxes. Make sure the lease payment is reasonable.

There you have it: Two new ways to fund your kids' college education and let the IRS pay a good portion of that cost. You are giving them money and you receive some tax benefits, too!

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