

# The DAILY PLAN-IT<sup>TM</sup>

## *Help self-employed clients understand if they qualify for a new 20-percent tax break*

The [Tax Cuts and Jobs Act](#) still has that new car smell, and it's providing advisors with a unique opportunity to help self-employed clients and small business owners reduce their tax burdens.

For entrepreneurs, one of the most exciting aspects of the new law is a 20 percent deduction for qualified business income from "pass through" entities, which include S corporations and limited liability companies.

You may have clients who are self-employed and are confused about whether they qualify for this new tax break or if they should restructure their business to reduce their tax burden.

### **Income threshold**

Under previous tax laws, business income would "pass through" to owners and was subject to individual income tax rates as high as 39.6 percent.

But now, business owners whose taxable annual income falls below certain levels can claim a 20 percent deduction, according to a [recent analysis piece by CNBC.com](#). The income thresholds are \$157,500 for individuals or \$315,000 for those who are married and file jointly.

Filers whose taxable income falls below those levels can take the deduction no matter what business they're in. However, when an entrepreneur's taxable income exceeds the threshold, some limitations are imposed. For example, entrepreneurs who own service businesses - including doctors, lawyers and financial advisors - might not be able to claim this deduction if their income is too high, *CNBC.com* reported.

In addition, partners inside a business might see a scenario in which one of them gets the 20 percent deduction but the other doesn't. This can happen when a partner with a high-income spouse surpasses the taxable income threshold.

### **Between the lines**

The new deduction is a "between the lines" deduction, meaning it does not lower a client's

adjusted gross income and he doesn't have to itemize it on his tax filing, *CNBC.com* reported.

If a client qualifies, the 20 percent break applies to the lesser of his qualified business income or his taxable income, minus capital gains.

It's important for your self-employed clients to understand how to tell the Internal Revenue Service to tax their businesses. Do they own a partnership or an LLC? If they are set up as an LLC, are they filing their taxes as an S-corp or a C-corp? What your client chooses matters for a variety of reasons.

### **Don't qualify? Get creative**

If a client's taxable income is too high to qualify for the 20 percent deduction, then there are some creative solutions that advisors can explore with them, [CNBC.com reported](#).

Saving more money for retirement may recapture these savings. The overall contribution limit for defined contribution plans is \$55,000 - that includes the \$18,500 employees can put into a 401(k). A self-employed person could put the maximum into a retirement plan to help lower his taxable income and get him under the threshold.

Another option for S-corp owners is to reduce the salary they collect and classify more of the business' money as "profit." The IRS provides [guidelines](#) as to what is a "reasonable" salary, and a client could justify a lower salary based on a wide range of factors.

If your self-employed clients have questions about structuring their business for tax purposes, how the new tax law affects them, or about making changes to their estate and business planning, we'd be happy to host a joint meeting with you at our office.

We hope this information is useful to you and helps your clients and their families. If you have a specific case or a question, please don't hesitate to call our office.

**©2018 All rights reserved.**

No portion of this newsletter may be reused in any way without prior express written consent.