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Hiring Your Child Can Have Advantages

By Karen E. Klein
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Q I have a small publishing company with no employees. However, lately I've needed some part-time help and wondered about hiring our college student son. What are the tax and employment rules for hiring a relative for occasional work?

A Hiring your kids can be a solution to the lack of qualified workers in today's marketplace. It also can be an effective income-shifting strategy between parents and children.

Most likely the wages you pay your son will be taxed at a lower rate than your income, or they may escape tax altogether if they are within the standard deduction of \$5,150 for 2006, said Bradford Hall, a certified public accountant and managing director of Irvine firm Hall & Co. (www.hallcpas.com).

"Be aware that the wages paid to your son need to be reasonable for the work being performed," he said.

"Reasonable wages are determined based on the following common factors: type of work to be performed, hours of services rendered and market rates."

Additionally, he said, you should maintain all records, including timesheets, showing that your son performed the services.

A major benefit of hiring your children is that given the right conditions, your company can realize huge savings on payroll taxes. Whether you'll be subject to payroll taxes depends on your son's age and your company's business structure.

If your son is younger than 18 and your company is a sole proprietorship, partnership or limited-liability company that you, your wife or you both own 100%, then the wages would be exempt from payroll taxes, Hall said.

But if the business is incorporated or you or your wife do not own 100% of the partnership or LLC, or your son is 18 or older, the company must withhold payroll taxes on wages paid, Hall said. In addition, you would have to pay the employer portion of the payroll taxes and federal and state unemployment insurance.

Social Security and Medicare withholding adds up to 7.65%. An employer must match that amount for a total cost of 15.3%.

If it makes sense for you to hire your son, you can have him contribute to an individual retirement account and may be able to put away as much as \$4,000 as an additional deduction for him. "This contribution is limited to the amount of earned income," Hall noted, "but between the standard deduction and an IRA contribution, your son, no matter his age, can earn up to \$9,150 in 2006 without having any income tax liability."

Have a question about running or starting a small enterprise? E-mail it to karen.e.klein@latimes.com or mail it to In Box, Los Angeles Times, 202 W. 1st St., Los Angeles, CA 90012.