

MONEY MYTHS SERIES

Hiring Your Kids to Cut Taxes: What the Rules and the Tax Court Allow (2026)

Which businesses get the payroll tax break for a child's wages, what the Tax Court allows, and California's extra rules for 2026.

By Eric Ridley, attorney, Ridley Law · Updated September 2026 · Read online with live links: ridleylawoffices.com/hire-your-kids-tax-benefits/

Part of our [money myths series](#), where we check what social media says about money against the statute, the IRS and the courts.

The claim: put your kids on payroll, pay each one up to the standard deduction, and the money comes out of your business tax-free, with no payroll tax. **The verdict:** the rule is real, and it gets stretched. The payroll tax break only applies to a business owned by the child's parents and not taxed as a corporation, the pay has to match real work at a market rate, and California is stricter than federal law for LLCs. The Tax Court has thrown out wages paid for chores, wages set equal to the standard deduction, and wages with no W-2.

Under 18

Age limit for the Social Security and Medicare exemption (IRC § 3121(b)(3)(A))

\$16,100

2026 standard deduction a working child can earn before federal income tax (Rev. Proc. 2025-32)

\$7,500

2026 IRA limit, capped at the child's earned pay (IRS, Nov. 2025)

\$0

Payroll tax break if the business is a corporation, including an S corp (IRS Pub. 15, 2026)

\$250

Per child per year the Tax Court allowed in Fisher (2016) against \$28,770 deducted

Hiring your kids is one of the more honest tax tips on social media, and it still gets people in trouble. The videos rarely say which businesses get the payroll tax break or what California adds. They also tend to show the best case, a parent in a high bracket paying a teenager the full standard deduction, as if every family could do it.

Who gets paid when you follow this advice

Done right, almost nobody, which is the good news. The costs are a payroll service and some paperwork. One payroll provider lists its price as "\$49 plus \$6 for each employee" a month.

The money shows up when "hire your kids" is sold as part of a package. In *Jadhav v. Commissioner*, T.C. Memo. 2023-140, a Texas couple paid a promoter \$50,000 for a 183-page "Income Tax Plan" that told them they could reduce their "average tax rate" to 9%. The plan stacked several moves, including renting their homes to their own company and "salaries to petitioners' children." Much of the plan failed in Tax Court, and the 2014 deficiency alone was \$265,990 with a \$53,198 penalty. The part that survived was the most ordinary one: the couple's adult sons were real employees, and their retirement contribution was allowed.

Is it legal to pay your kids from your business?

Yes, if the child does real work for the business and the pay is reasonable for that work. IRC § 162(a)(1) allows "a reasonable allowance for salaries or other compensation for personal services actually rendered."

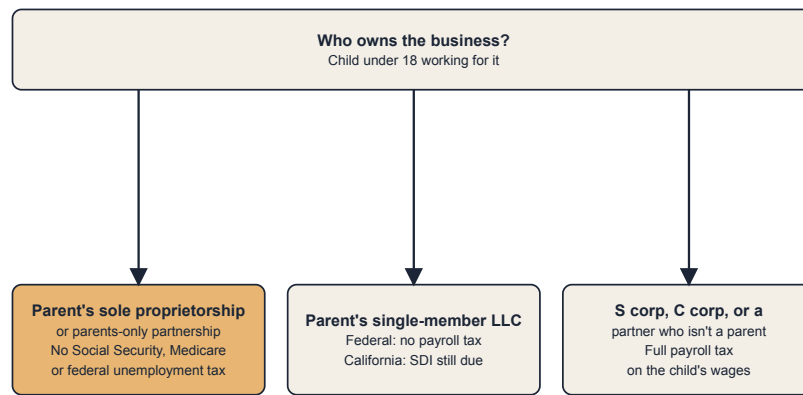
The Treasury regulation adds the test courts use: the pay must be reasonable and "in fact payments purely for services," measured by what similar businesses pay for similar work. A child who files, scans, answers phones, cleans a shop, or makes social media posts for the business can be a real employee. A child who does household chores can't, no matter what the payroll records say.

When does a child's pay skip Social Security, Medicare and unemployment tax?

When the child is under 18 and works for a business owned only by the child's parents, either as a sole proprietorship or a partnership in which every partner is a parent (IRS Publication 15, 2026).

IRC § 3121(b)(3)(A) excludes "service performed by a child under the age of 18 in the employ of his father or mother" from Social Security and Medicare, and § 3306(c)(5) excludes a child under 21 from federal unemployment tax. Publication 15 lists who doesn't qualify: "A corporation, even if it is controlled by the child's parent," and "A partnership, even if the child's parent is a partner, unless each partner is a parent of the child." So an S corporation, the entity many of these videos recommend for other reasons, gets no payroll tax break for the kids. A single-member LLC owned by a parent and taxed as a sole proprietorship does qualify federally, because the regulations treat the owner as the employer.

Income tax is different. The IRS says payments to a child "are subject to income tax withholding regardless of age." The benefit is that the child's own standard deduction usually brings that tax to zero.



How much can you pay your child tax-free in 2026?

Up to \$16,100 of wages for 2026 with no federal income tax to the child, because a dependent's standard deduction is their earned income plus \$450, capped at the regular \$16,100 standard deduction (Rev. Proc. 2025-32).

That number is a ceiling for the child's tax, not a target for the pay. The pay still has to match the work. In *Alexander v. Commissioner*, T.C. Summ. Op. 2006-127, parents credited each of three daughters, ages 17, 9 and 8, with \$4,250 for helping in a dog-breeding business. The court pointed out that "\$4,250 was the amount of the standard deduction in 1998" and treated it as a predetermined flat amount, not pay for hours worked. No W-2s had been issued. The deduction was disallowed except for \$455 the IRS had allowed on its own.

A child with earned income can also open a Roth IRA. The 2026 IRA limit is \$7,500, but contributions can't exceed the child's taxable compensation for the year.

What has the Tax Court said about paying your kids?

It allows real pay for real work and disallows the rest. In *Eller v. Commissioner*, 77 T.C. 934 (1981), a California family won most of the deduction, while families paying for chores or round numbers have lost almost all of it.

Eller (1981), the case the videos rely on. A family in Soquel, California, paid three children, ages 12, 11 and 7, for work at the family's trailer parks and other businesses. The IRS disallowed about 90%. The court allowed most of it, finding the children "performed substantial services" worth \$4,727, \$3,652 and \$7,168, because without them "a third party (or parties) would have had to have been hired."

Denman (1967). An engineer paid his sons, ages 7 to 11, for errands, snow shoveling, mowing and window washing. The court called the work mainly "parental training and discipline" and cut the deduction for 1960 from \$1,560 to \$185. He also had no work permits for the boys.

Embroidery Express (2016). A business paid its owners' children regular wages, plus large December payments. The court allowed the regular monthly pay, including a full-time 17-year-old receptionist's wages. But a 10-year-old who was paid \$1,050 over 11 months and then a \$10,000 check on December 22 got only \$350 of that check

allowed. The court said the bonuses looked like family support, not wages (T.C. Memo. 2016-136).

Fisher (2016). Parents deducted \$10,435, \$10,313 and \$8,022 in "wages to minor children" over three years for kids who were all under 9. There were no W-2s and no payroll records. The court allowed \$250 per child per year and applied a negligence penalty to the rest (T.C. Summ. Op. 2016-10).

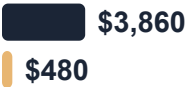
Ross (2014). The "wages" were mostly the parent's credit card charges for pizza, tutoring and cash withdrawals. The court disallowed them and listed the warning signs it looks for: no payroll filings, a flat amount set at the start of the year, pay that doesn't track work, no records, and pay for family chores (T.C. Summ. Op. 2014-68).

■ Deducted ■ Allowed

Eller (1981), California, won



Denman (1967)



Fisher (2016)



Alexander (2006), daughters



Embroidery Express (2016), age 10



Totals over the years at issue in each case. Eller: three children, 1972 to 1974. Denman: 1957 to 1960. Fisher: three children, three years.

Case	Deducted	Allowed	Why
Eller v. Commissioner, 77 T.C. 934 (1981)	\$17,697	\$15,547	Real work a third party would have been paid to do
Denman v. Commissioner, 48 T.C. 439 (1967)	\$3,860	\$480	Chores were "parental training and discipline"
Fisher, T.C. Summ. Op. 2016-10	\$28,770	\$2,250	Kids under 9; no W-2s or payroll records
Alexander, T.C. Summ. Op. 2006-127	\$12,750	\$455	Flat amount equal to the standard deduction; no W-2s

Case	Deducted	Allowed	Why
Embroidery Express, T.C. Memo. 2016-136 (10-year-old, 2006)	\$11,050	\$1,400	\$10,000 December check treated as family support

What does California add?

California excludes a parent's under-18 child from state unemployment and disability tax only if the business isn't a corporation or an LLC, and it can require a work permit (EDD form DE 231FAM; Education Code § 49141).

The state exclusion in Unemployment Insurance Code § 631 mirrors the federal one, but the Employment Development Department says it "does not apply if the employing entity is a limited liability company," and it doesn't apply to corporations either. So a parent-owned California LLC can skip federal payroll tax on a child's wages and still owe California SDI, which is 1.3% of all wages in 2026. The child's wages remain subject to California income tax withholding and reporting.

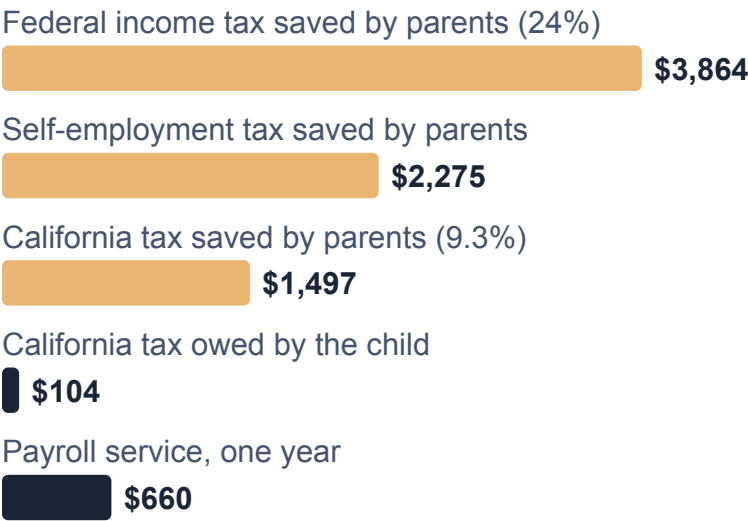
California also has work permit rules. The state generally requires a permit for any minor under 18. A parent's own business is exempt when the child works on premises the parent controls, but that exemption doesn't reach "manufacturing, mercantile, or similar commercial enterprises." A child stocking shelves in a parent's retail store may still need a permit.

Worked example: a 15-year-old on payroll in 2026

The numbers here are hypothetical and simplified. A married California couple runs a sole proprietorship and is in the 24% federal bracket and the 9.3% California bracket. Their 15-year-old works real hours in the business, at a market rate, and earns \$16,100 for the year.

- **Federal income tax the parents save:** 24% of \$16,100, or \$3,864.
- **Self-employment tax the parents save:** about \$2,275 (15.3% on 92.35% of the wages), because the business profit drops and the child's pay isn't subject to Social Security or Medicare.
- **California tax the parents save:** 9.3% of \$16,100, or \$1,497.
- **What the child owes:** \$0 federal. About \$104 in California, because California's standard deduction for a dependent was \$5,706 for 2025 and a dependent can't claim the personal exemption credit.
- **Payroll cost:** about \$660 a year at one provider's list price.

Net, the family keeps roughly \$6,900 more than without the job, and the money belongs to the child. If the same family operated as an S corporation, about \$2,463 (15.3% of \$16,100) of combined Social Security and Medicare tax would come back. If the deduction were disallowed, as in Fisher, the parents would owe the \$6,139 of federal tax back, a 20% penalty of about \$1,228, the California tax, and interest. The example ignores the qualified business income deduction and the deduction for half of self-employment tax, both of which would shrink the federal savings.



Hypothetical and simplified: ignores the qualified business income deduction and the deduction for half of self-employment tax. California uses 2025 rates; 2026 schedules not yet published.

Item	Amount
Federal income tax saved by parents (24%)	\$3,864
Self-employment tax saved by parents	\$2,275
California tax saved by parents (9.3%)	\$1,497
California tax owed by the child	\$104
Payroll service, one year	\$660
Net to the family	\$6,872

When does hiring your kids make sense?

When you'd pay someone to do the work anyway, your child can do it, and you're willing to run real payroll for them.

The family in Eller won because the work was work: a third party would have been hired otherwise. A teenager who handles your scheduling, edits your videos or keeps your books is a better fit than a 6-year-old "model" whose pay happens to equal the standard deduction. The money is legally the child's, so it should go to the child, into the child's own account, a Roth IRA or a 529 plan, not back into the family checking account.

What the video says	What the law says
"Pay each kid \$16,100 tax-free."	\$16,100 is the most a child can earn in 2026 before federal income tax. The pay still has to match the work.
"No payroll taxes."	Only for a business owned by the parents and not taxed as a corporation. S corps pay Social Security and Medicare on the kids too.
"Works for any LLC."	Federally, a parent-owned single-member LLC qualifies. California still charges SDI on LLC wages.

What the video says	What the law says
"Chores count."	Courts treat chores as "parental training and discipline," not work for the business.
"You don't need a W-2."	No W-2s was a reason the deduction failed in Fisher and Alexander.
"Pay them in December."	A \$10,000 year-end check to a 10-year-old was cut to \$350 in Embroidery Express.

What should you do instead?

Do it the way the winning families did: a real job, real pay, real records.

- 1 Write a job description**
Tasks a business pays for, at a rate you'd pay a stranger of the same age and skill. Age-appropriate work only.
- 2 Track hours and pay on a schedule**
Timesheets and regular pay periods. No lump sums at year-end, no flat amounts set in January.
- 3 Run payroll**
Withholding forms, a W-2 and California employer reporting. Check whether a work permit is needed.
- 4 Check the entity**
If you're an S corp, the payroll tax break is gone. If you're a California LLC, SDI still applies. See [LLC vs. S corp in California](#).
- 5 Pay the child, not the household**
Deposit the wages in the child's account. If you want to save for them without a job, a 529 plan works, and the 2025 budget law created "Trump accounts" with a \$5,000 annual limit for children under 18.

Hiring your kids is often pitched alongside other family-business moves. See [the Augusta rule](#), [the "LLC write-off"](#), our [family business succession](#) page and [college savings and estate plans](#).

Frequently asked questions

How old does my child have to be to work in my business?

There's no minimum age in the tax code, but the work has to be real and age-appropriate. Courts have rejected pay to very young children for chores. Federal child labor law lets a parent employ a child under 16 outside mining, manufacturing and hazardous jobs.

Do I have to file a W-2 for my child?

For 2026 wages, a W-2 is required when wages reach \$2,000 and no tax was withheld, a threshold the 2025 budget law raised. File one anyway. The Tax Court has treated missing W-2s as evidence the child wasn't a real employee.

Does my S corporation get the payroll tax exemption for my kids?

No. Publication 15 says a corporation doesn't qualify "even if it is controlled by the child's parent." The S corp can still deduct reasonable wages, but it pays Social Security and Medicare on them.

Can my child put their wages in a Roth IRA?

Yes, up to the lesser of \$7,500 for 2026 or the child's taxable compensation. There's no minimum age for IRA contributions.

Does California charge payroll tax on my child's wages?

Not for unemployment and disability insurance if the business is a sole proprietorship or parents-only partnership and the child is under 18. It does if the business is an LLC or a corporation. California income tax withholding rules apply either way.

Can I still claim my child as a dependent if I pay them?

Yes, as long as the other tests are met. One of them is that the child can't provide more than half of their own support, which is another reason the wages should be saved, not spent on the child's living costs.

What happens if the IRS disallows the wages?

The deduction is reversed, you owe the tax and interest, and you may owe a 20% accuracy penalty. In *Fisher* the court allowed \$250 per child per year and applied a negligence penalty to the rest.

This page is general information, not legal, tax or investment advice for your situation. Payroll for family members has state and federal rules that turn on your entity type, so set it up with your own tax preparer or payroll provider.

More in the [money myths](#) series.

SOURCES

- 26 U.S.C. § 3121(b)(3)(A), [Cornell LII](#); 26 U.S.C. § 3306(c)(5), [Cornell LII](#); 26 U.S.C. § 162(a)(1), [Cornell LII](#); 26 U.S.C. § 152, [Cornell LII](#); 29 U.S.C. § 203(l), [Cornell LII](#).
- Treas. Reg. § 31.3121(b)(3)-1, [eCFR](#); Treas. Reg. § 1.162-7, [eCFR](#).
- IRS, [Family employees](#), updated October 10, 2025; [Publication 15 \(Circular E\)](#), [Employer's Tax Guide](#), 2026.
- IRS, [Rev. Proc. 2025-32](#), October 2025; [401\(k\) limit increases to \\$24,500 for 2026](#), [IRA limit increases to \\$7,500](#), November 13, 2025; [IRA contribution limits](#), updated September 2026; [Self-employment tax](#).
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- Cal. Unemp. Ins. Code § 631; Cal. Educ. Code §§ 49141, 49160; Cal. Lab. Code §§ 1299, 1394, [California Legislative Information](#); IWC [Wage Order 4](#).
- California EDD, [DE 231FAM, Types of Employment: Family Employment](#); [2026 rates and withholding](#).
- Franchise Tax Board, [2025 tax rate schedules, deductions and 2025 Form 540 booklet](#).
- *Eller v. Commissioner*, 77 T.C. 934 (1981), [CourtListener](#).
- *Denman v. Commissioner*, 48 T.C. 439 (1967), [CourtListener](#).
- *Embroidery Express, LLC v. Commissioner*, T.C. Memo. 2016-136, [CourtListener](#).

- Fisher v. Commissioner, T.C. Summ. Op. 2016-10 (nonprecedential), [CourtListener](#).
- Ross v. Commissioner, T.C. Summ. Op. 2014-68 (nonprecedential), [CourtListener](#).
- Alexander v. Commissioner, T.C. Summ. Op. 2006-127 (nonprecedential), [CourtListener](#).
- Jadhav v. Commissioner, T.C. Memo. 2023-140, [CourtListener](#).
- OnPay, [pricing page](#), accessed October 7, 2026 (vendor marketing).

Questions about your own plan?

Ridley Law helps California families with trusts, wills, trust administration and probate from Port Hueneme, serving Ventura, Santa Barbara and Los Angeles counties. The first call is free and runs 30 minutes.

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