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OCTOBER 2016

BILL GERARDY TO RETIRE

C. William Gerardy, Jr., CPA has announced his retirement effective December 31, 2016. Bill joined the firm in 1972 after completing his accounting education at Centenary College, rapidly became a highly competent CPA and, on July 1, 1978, became a very valued partner. In a day when people move about frequently, Bill is proud to say that he has spent his entire adult working life and career with the firm.

Bill's career is evidence supporting our long-held conclusion that success in public accounting is readily available to those who maintain mastery of the prerequisite professional knowledge and who work diligently to provide quality service to clients. Bill Gerardy epitomizes professional competence and commitment to clients. His 44 years of public accounting service contributed greatly to the well-being of clients, the firm, and the larger community. We are indebted to Bill for his long service and we will miss his competency and dedication to our clients and to the firm. We are happy for him and wish for him a successful retirement.

FUND EARLY AND FULLY

Most of us are aware of the favorable long-term effects of tax-deferred compounding on accumulations within IRAs, pension and profit-sharing plans, etc. For example, an annual investment of $5,500 on the last day of each year of a 20-year accumulation cycle results in $257,051 at 8.19 percent (the return of the S&P 500 Index over the 20 years ended December 31, 2015). An investment on the first day of each year of a 20-year period compounded at the same 8.19 percent accumulates to $278,103. Thus, the annual early funding of a tax-deferred plan or IRA resulted in an increase of $21,052 or over eight percent in the ultimate accumulation under the above assumptions. Accordingly, when funds are available, we strongly recommend the full funding of all available tax-favored accounts at the earliest possible time. While company-sponsored plans (e.g. 401(k), profit-sharing, etc.) might not be available to everyone, every individual (including dependents) under age 70½ with earned income can choose to fund a traditional or Roth IRA.

Marginal income tax rates have increased for those paying most of the income tax. Payroll tax rates have increased on all earned income, and new Medicare taxes on certain earned income and investment income are in effect for 2016. Accordingly, we are evermore convinced of the benefits of tax-deferred or tax-free (Roth) income accumulations in obtaining financial security. The limits on contributions to tax-favored plans and IRAs for 2016 are as shown on the reverse:

(Continued on reverse)

2016 Limitations

401(k) Maximum Elective Deferral:	
Below Age 50	$18,000
Age 50 or Above	$24,000
Maximum Contribution to Defined Contribution Retirement Plan:	
General Limit – All Plans	$53,000
With 401(k) Feature (Age 50 and over)	$59,000
Individual Retirement Account Contribution (IRAs):	
Below Age 50	$ 5,500
Age 50 or Above	$ 6,500
SIMPLE IRA Maximum Deferral:	
Below Age 50	$12,500
Age 50 or Above	$15,500

We would be pleased to answer any questions you might have about tax-favored savings plans.

RAPID TAX WRITE-OFFS – CAPITAL EXPENDITURES

Those considering the near-term purchase of business-use assets will want to understand the available tax benefits of bonus depreciation (50 percent immediate deduction) and the Section 179 expense election (100 percent immediate deduction). Both are available for 2016 and for 2017.

Bonus Depreciation

One-half of the cost of qualified new property (used property is not eligible) can be deducted in the year purchased and placed in service. This 50% bonus depreciation deduction is available for assets first used in 2016 or 2017. Property qualified for the deduction generally includes all new tangible property that is depreciable over 20 years or less, such as equipment, fences, land improvements, farm buildings, and billboards. Bonus depreciation at the 50 percent rate is also available for most improvements to the interior portions of non-residential buildings.

Immediate Deduction in Full

Many asset purchases (either new or used property) acquired for business use can be deducted in the year purchased. This special expensing election (Section 179 deduction) is available for up to $500,000 of qualifying purchases. The deduction is limited if more than $2,000,000 of fixed assets are purchased in a year. Unlike bonus depreciation, the annual Section 179 deduction is limited to the amount of aggregate taxable business income for the year.

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Tax & Business Alert

OCTOBER 2016

TAKE THE WORRY OUT OF BUSINESS VALUATIONS

Appraisals can inspire anxiety for many business owners. And it's understandable why. You're obviously not short on things to do, and valuations cost time and money. Nonetheless, there are some legitimate reasons to obtain an appraisal regularly or, at the very least, to familiarize yourself with the process so you're ready when the time comes.

STRATEGIC PERSPECTIVES

Perhaps the most common purpose of a valuation is a prospective ownership transfer. Yet strategic investments (such as a new product or service line) can also greatly benefit from an accurate appraisal. As growth opportunities arise, business owners have only limited resources to pursue chosen strategies. A valuation can help plot the most likely route to success.

But hold on — you might say, why not simply rely on our tried-and-true projected financial statements for strategic planning? One reason is that projections ignore the time value of money because, by definition, they describe what's *going to* happen given a set of circumstances. Thus, it can be difficult to compare detailed projections against other investments under consideration.

Valuators, however, can convert your financial statement projections into cash flow projections and then incorporate the time value of money into your decision making. For instance, in a net present value (NPV) analysis, an appraiser projects each alternative investment's expected cash flows. Then he or she discounts each period's projected cash flow to its present value, using a discount rate proportionate to its risk.

If the sum of these present values — the NPV — is greater than zero, the investment is likely worthwhile. When comparing alternatives, a higher NPV is generally better.

3 PILLARS OF THE PROCESS

Many business owners just don't know what to expect from a valuation. To simplify matters, let's look at three basic "pillars" of the appraisal process:

1. Purpose. There's no such thing as a recreational valuation. Each one needs to have a specific purpose. This could be as clear-cut as an impending sale. Or perhaps an owner is divorcing his spouse and needs to determine the value of the business interest that's includable in the marital estate.

In other cases, an appraisal may be driven by strategic planning. Have I grown the business enough to cash out now? Or how much further could we grow based on our current estimated value? The valuation's purpose strongly affects how an appraiser will proceed.

2. Standard of value. Generally, business valuations are based on "fair market value" — the price at which property would change hands in a hypothetical transaction involving informed buyers and sellers not under duress to buy or sell. But some assignments call for a different standard of value.

For example, say you're contemplating selling to a competitor. In this case, you might be best off getting an appraisal for the "strategic value" of your company — that is, the value to a particular investor, including buyer-specific synergies.

3. Basis of value. Private business interests typically are designated as either "controlling" or "minority" (nonmarketable). In other words, do you truly control your company or are you a noncontrolling owner?

Defining the appropriate basis of value isn't always straightforward. Suppose a business is split equally between two partners. Because each owner has some control, stalemates could impair decision-making. An appraiser will need to definitively establish basis of value when selecting a valuation methodology and applying valuation discounts.

UNBIASED PERSPECTIVE

Often, we all find it difficult to be objective about the things we hold close. There are few better examples of this than business owners and their companies. But a valuation can provide you with an unbiased, up-to-date perspective on your business that can help you make better decisions about its future. ■

OWNER-EMPLOYEES FACE DISTINCTIVE TAX PLANNING CHALLENGES

Many business owners launch their companies from the front lines — as an employee. And it's not uncommon for owners to stay in that role, working with their staff members to grow the business and guide its strategic direction. Come tax time, however, owner-employees face a variety of distinctive tax planning challenges.

PARTNERSHIPS AND LLCs

If you're a partner in a partnership or a member of a limited liability company (LLC) that has elected to be disregarded or treated as a partnership, the entity's income (and deductions) flow through to you. Trade or business income that flows through to you for income tax purposes likely will be subject to self-employment taxes — even if the income isn't actually distributed to you.

You'll also need to assess whether the additional 0.9% Medicare tax on earned income or the 3.8% net investment income tax (NIIT) will apply. Doing so will involve complex determinations.

CORPORATIONS

For S corporations, even though the entity's income flows through to you for income tax purposes, only income you receive as salary is subject to employment taxes and, if applicable, the 0.9% Medicare tax. To reduce these taxes, you may want to keep your salary relatively — but not unreasonably — low and increase your distributions of company income (which generally isn't taxed at the corporate level or subject to employment taxes). The 3.8% NIIT may also apply.

In the case of C corporations, the entity's income is taxed at the corporate level and only income you receive as salary is subject to employment taxes, and, if applicable, the 0.9% Medicare tax. Nevertheless, if the overall tax paid by both the corporation and you would

TAX CALENDAR

October 17

- Personal returns that received an automatic six-month extension must be filed today and any tax, interest, and penalties due must be paid.
- Electing large partnerships that received an additional six-month extension must file their Forms 1065-B today.
- If the monthly deposit rule applies, employers must deposit the tax for payments in September for Social Security, Medicare, withheld income tax, and nonpayroll withholding.

October 31

- The third quarter Form 941 ("Employer's Quarterly Federal Tax Return") is due today and any undeposited tax must be deposited. (If your tax liability is less than $2,500, you can pay it in full with a timely filed return.) If you deposited the tax for the quarter in full and on time, you have until November 10 to file the return.
- If you have employees, a Federal Unemployment Tax Act (FUTA) deposit is due if the FUTA liability through September exceeds $500.

November 15

- If the monthly deposit rule applies, employers must deposit the tax for payments in October for Social Security, Medicare, withheld income tax, and nonpayroll withholding.

December 15

- Calendar-year corporations must deposit the fourth installment of estimated income tax for 2015.
- If the monthly deposit rule applies, employers must deposit the tax for payments in November for Social Security, Medicare, withheld income tax, and nonpayroll withholding.

be less, you may prefer to take more income as salary (which is deductible at the corporate level) as opposed to dividends (which aren't deductible at the corporate level, are taxed at the shareholder level and could be subject to the 3.8% NIIT).

Tread carefully, however. The IRS remains always on the lookout for misclassification of corporate payments to shareholder-employees. The penalties and additional tax liability can be costly.

THE SELF-EMPLOYED

If you're self-employed (such as a sole proprietor, partner or LLC member treated as either of them), your business earnings are subject to self-employment taxes. This means your employment tax liability typically doubles, because you must pay both the employee and employer portions of these taxes. The employer portion of self-employment taxes paid (6.2% for Social Security tax and 1.45% for Medicare tax) is deductible above the line.

As a self-employed taxpayer, you may benefit from other above-the-line deductions as well. You can deduct 100% of health insurance costs for yourself, your spouse and your dependents, up to your net income from the business. You also can deduct contributions to a retirement plan.

Above-the-line deductions are particularly valuable because they reduce your adjusted gross income and modified adjusted gross income, which are the triggers for certain additional taxes and phaseouts of many tax breaks.

IDEAL STRATEGIES

Owning and working for your own company can be incredibly fulfilling. But tax planning is extra important when you take on this role. Please call us for help identifying the ideal strategies for your situation. ■

HAVE A PENSION? BE SURE TO PLAN CAREFULLY

The traditional pension may seem like a thing of the past. But many workers are still counting on payouts from one of these "defined benefit" plans in retirement. If you're among this group, it's important to start thinking now about how you'll receive the money from your pension.

MAKING A CHOICE

Some defined benefit plans give retirees a choice between receiving payouts in the form of a lump sum or an annuity. Taking a lump sum distribution allows you to invest the money as you please. Plus, if you manage and invest the funds wisely, you may be able to achieve better returns than those provided by an annuity.

On the other hand, if you're concerned about the risks associated with investing your pension benefits (you could lose principal) — or don't want the responsibility — an annuity offers guaranteed income for life. (Bear in mind that guarantees are subject to the claims-paying ability of the issuing company.)

CHOOSING YET AGAIN

If you choose to receive your pension benefits in the form of an annuity — or if your plan doesn't offer a lump sum option — your plan likely will require you to choose between a single-life or joint-life annuity. A single-life annuity provides you with monthly benefits for life. The joint-life option (also referred to as "joint and survivor") provides a smaller monthly benefit, but the payments continue over the joint lifetimes of both you and your spouse.

Deciding between the two annuity options requires some educated guesswork. To determine the option that will provide the greatest overall financial benefit, you'll need to consider several factors — including your and your spouse's *actuarial* life expectancies as well as factors that may affect your *actual* life expectancies, such as current health conditions and family medical histories.

You might choose the single-life option, for example, if you and your spouse have comparable life expectancies or if you expect to live longer. Under those circumstances, the higher monthly payment will maximize your overall benefits.

But there's a risk, too: Because the payments will stop at your death, if you die prematurely and your spouse outlives you, the overall financial benefit may be smaller than if you'd chosen the joint-life option. The difference could be substantial if your spouse outlives you by many years.

Your overall financial situation — that is, your expenses and your other assets and income sources — also play a major role. Even if you expect a joint-life annuity to yield the greatest total benefit over time, you may want to consider a single-life annuity if you need additional liquidity in the short term.

MANAGING THIS ASSET

Although increasingly uncommon, these defined benefit plans can be a highly valuable asset. Please contact us for help managing yours appropriately. ■

TIMING IS EVERYTHING: YOUR INCOME AND EXPENSES

They say timing is everything. And, when it comes to year-end tax planning, this expression certainly holds true for income and expenses.

KNOW THE BASICS

When you don't expect to be subject to the alternative minimum tax this year or next, deferring income to next year and accelerating deductible expenses into the current year typically is wise. Why? Because it will defer tax, which is usually beneficial.

But when you expect to be in a higher tax bracket next year — or you expect tax rates to go up — the opposite approach may be beneficial: Accelerating income will allow more income to be taxed at your current year's lower rate. And deferring expenses will make the deductions more valuable, because deductions save more tax when you're subject to a higher tax rate.

Also, don't forget to take into account the income-based itemized deduction reduction when considering timing strategies.

IDENTIFY THE ITEMS

As you undertake effective timing, identify items that you may be able to control. Controllable *income items* typically include bonuses and consulting or other self-employment income. For, example, if you own a cash-basis business, you might send out December invoices early (to receive income in 2016) or late (to receive it in 2017).

Potentially controllable *expenses* usually include:

- Business expenditures and certain retirement plan contributions, if self-employed,
- State and local income taxes,
- Property taxes, and
- Charitable contributions.

Bear in mind that, generally, prepaid expenses can be deducted only in the year to which they apply.

PICK YOUR PARTNER

Timing is easier with a good dance partner. We can help you identify your controllable items and decide whether to defer or accelerate. ■