Ideas & Trends

SUMMER 2017

Asset protection
Shielding your individual wealth today

Business valuations: A learning process

Is your business taking advantage of the R&D tax credit?

How to reap tax benefits from a summer vacation

Israeloff, Trattner & Co., P.C.
CERTIFIED PUBLIC ACCOUNTANTS • FINANCIAL CONSULTANTS

1225 Franklin Avenue • Garden City, NY 11530
450 Seventh Avenue • New York, NY 10123
www.israeloff.com • 800-945-0200

Asset protection

Shielding your individual wealth today

Like many affluent individuals, you've probably worked hard for years to accumulate assets and create wealth. But have you taken steps to protect your hard-earned assets?

Asset preservation is as important as asset accumulation in today's increasingly litigious society. Depending on how your wealth is structured and how your assets are invested, a single personal injury lawsuit could wipe out everything you've accumulated over your lifetime. Consider the following issues as you initiate actions to protect your individual assets.

WHAT'S YOUR LOSS EXPOSURE?

The first step in safeguarding what you own is determining your potential loss exposure. In other words, how much do you possess that could be claimed and seized by creditors in a legal judgment? Based on that information, you can devise strategies to reduce your loss exposure. Most strategies to lessen your exposure fall into one of these categories:

Liability insurance. This is one of the first levels of asset protection for individuals. Liability insurance policies help protect your assets from the financial risks associated with personal liability resulting from an adverse legal judgment.

Auto and homeowner's policies, for example, usually include some liability coverage. Upping your liability coverage beyond the standard amounts (typically from $10,000 to $25,000) will provide additional asset protection.

Personal liability umbrella insurance will provide even more liability coverage above the limits of your auto and homeowner's policies. For instance, if you were sued for causing a car accident or found liable for injuries suffered by a visitor to your home, umbrella insurance would provide coverage up to the policy limits (such as $1 million).

Statutory asset protection from creditors. Federal or state law exempts certain kinds of property and assets from creditor liens. Thus, some assets you

own will automatically be protected due to statutory guidelines. Qualified retirement plans are this type of asset, as are IRAs and 401(k) plans, life insurance proceeds and Section 529 college savings plans. But keep in mind that *inherited* assets may not have the same degree of protection.

The amount of home equity that is protected (generally called the "homestead exemption") depends on state law. In some states it's very generous, but in others it's extremely limited, given the value of homes today. Consult with your attorney about your particular situation in your particular state.

Asset ownership structure. Ownership of your assets will play an important role in whether or not they can be seized by creditors. Thus, it might be wise in some situations to transfer ownership of certain assets to your spouse. If you're at a high risk of liability — for example, you're a business owner — one strategy might be to retain ownership of assets with statutory protection, as mentioned above, and transfer ownership of all other assets to your spouse.

Trusts. Irrevocable trusts also can be used as an asset protection tool. Assets placed in an irrevocable trust can't be removed. Nor can the trust terms be changed. With this step, you've effectively relinquished control over the assets, thus putting them out of reach of your creditors. The asset transfer must be done in advance of the act that created the liability, or the transfer could be nullified. In other words, the time to think about setting up such a trust is before you need to take advantage of it.

An irrevocable trust also can help you protect assets for your children and grandchildren. Consider structuring the trust in a way that effectively gives future generations the benefit of the assets without transferring ownership of them to your heirs. This can shield those assets from your descendants' future creditors.

The role of domestic asset protection trusts

One of the most common strategies for protecting assets from creditors is placing them in a domestic asset protection trust. This is a special type of irrevocable trust that, in most situations, shields assets from attachment by creditors in the future.

Assets held in this type of trust generally can't be seized by creditors as a result of a personal liability judgment due to an accident that causes injury (such as a car wreck) or a divorce settlement. Physicians, business owners, CEOs, corporate directors, professional athletes and entertainers are among the individuals who can benefit the most from this type of trust.

Domestic asset protection trusts also can be used as an alternative to a prenuptial agreement, provided the trust was created and funded in advance of the marriage. Practically any kind of asset can be transferred into the trust, including cash, business ownership interest, real estate, and stocks and bonds. You'll relinquish some control over assets placed in the trust, but you'll also retain certain rights — for example, the ability to receive distributions.

If you decide to use trusts as part of your asset protection strategy, remember that they may be subject to higher tax rates and additional tax filing requirements. Trusts also may be costly to set up and require expert legal counsel to administer and maintain.

OBTAIN EXPERT ASSISTANCE

The details involved in implementing asset protection strategies can be complex. Talk with your attorney and financial advisor to obtain guidance in your particular case. •

Business valuations: A learning process

Do you think of the professional valuation of your business as a necessary step only when you're ready to sell your business? While that's one purpose, don't be short-sighted: A valuation can serve many ends during the time you own your company.

FROM FINANCING TO A BETTER UNDERSTANDING

Although the economy is relatively healthy, it still poses plenty of challenges for many U.S. companies. Chief among these is financing — it's not easy to secure because lenders imposed tough standards after the last recession.

A business valuation conducted by an outside expert can help you present lenders with timely, in-depth financial data. Not only will it make it easier for bankers to understand how your business runs, but the discounted cash flow section will show how your expected future cash flows will build value. This can go a long way toward easing lender concern about your ability to compete in the marketplace.

When performing a valuation of your business, a valuator will likely examine several company-specific factors, including:

- Your and your managers' awareness of market conditions,
- What specific risks you face, and
- Your contingency planning efforts to mitigate these risks.

As you undergo a valuation, you may discover another plus from the process. You might recognize some of your company's weaknesses. You can then devise ways to strengthen them.

HOW A BUY-SELL AGREEMENT ENTERS IN

As a business owner, you never know what proverbial winds may blow your way. For example, your partner might want to leave the business at an unexpected time. He or she might decide to retire early, or need to cash out for personal reasons. Or health concerns may enter the picture.

For all of these reasons and more, it's important to draft and maintain a buy-sell agreement. This contract among a business's owners sets guidelines for the transfer of their ownership interests. The agreement gives the remaining owners (or the business itself) the right to buy an exiting owner's interest if a "triggering" event takes place. Such events may include an owner's desire to leave the company, divorce, disability, retirement, death, or loss of a professional license or certification.

So what does all of this have to do with a business valuation? A valuation of your company plays a key role in the creation and maintenance of a buy-sell agreement. Specifically, it could help you address the preferred valuation method, the appropriate standard of value, the effective valuation date, and the applicability of valuation discounts and premiums.

A WEATHER VANE

There's no getting around the fact that a key reason for getting a valuation is to prepare for a business transfer. Even if you aren't sure you want to buy, sell or gift a business interest, an evaluation may help you get a better sense of whether now is the time.

Most valuators subscribe to transaction databases that report recent selling prices of similar private businesses. In conjunction with input from other professionals, the information gleaned from the valuation can help you come up with a creative deal structure — one that minimizes taxes, provides you with income to fund retirement and meets other transfer objectives.

ESTABLISHING CREDIBILITY

Additionally, in the eyes of a potential buyer, a formal evaluation adds credibility to your asking price.

And if you're gifting business interests, it's a must-have to survive IRS scrutiny.

Alternatively, if you're in a position to buy out a competitor or other business, a valuation should play a critical role in your due diligence. An evaluator can scrutinize the seller's asking price, including the reasonableness of cash flow and risk assumptions, when negotiating the final sale price.

NEVER TOO EARLY

Even if you're not buying or selling a business now, it's not too early to go through the valuation process. Your CPA will be able to recommend a valuation professional. •

Is your business taking advantage of the R&D tax credit?

Savvy business owners are always on the lookout for valuable tax breaks. One potentially lucrative tax break often overlooked by businesses is the research and development (R&D) tax credit.

Unfortunately, some business owners think that the R&D tax credit is available only to technology firms or large corporations. But this isn't the case: Any size company in any industry can claim the credit if it meets certain criteria.

THE FOUR-PART TEST

A simple test can determine whether or not your business qualifies for the R&D tax credit. To qualify, your business must perform activities that meet at least one of these four criteria:

1. They attempt to eliminate technical uncertainty associated with the development or improvement of a product or process.
2. They try to resolve a technical uncertainty by conducting simulations, modeling, hypothesis testing or another method of experimentation.
3. They are technological in nature and based on sound principles of the hard sciences, such as engineering, physical science or computer science.
4. They result in the creation of a new or improved product or process, such as increased performance, functionality, quality or reliability.

Within these parameters, there's a wide range of activities that could qualify for the R&D tax credit. These include, but aren't limited to, software development, certification testing, automated manufacturing processes, design tools, patents, and dies and molds.

If your company has no taxable income in a particular year, you can carry R&D tax credits forward for up to 20 years to offset taxable income in the future. You also can claim the credit retroactively for the past three years by filing amended returns.

PERMANENCE AND OFFSETS

After many years of being retroactively extended at year end, the R&D tax credit was finally made permanent in a law passed in December 2015, effective for 2016 tax returns. In addition, new offsets were added that could make the R&D tax credit even more valuable.

One of these is a payroll tax offset for certain start-ups that have gross receipts for five years or less and average gross receipts of less than $5 million during this time. If such companies don't owe any income tax in a particular year, they can use the R&D tax credit to offset up to $250,000 in payroll taxes.

> *New offsets were added that could make the R&D tax credit even more valuable.*

Additionally, businesses with $50 million or less in gross receipts can claim the credit against alternative minimum tax (AMT) liability.

THINK IT OVER

If you didn't think your business could qualify for the R&D tax credit, it may be time to think again. Talk with your tax advisor about the potential benefits of this valuable tax saver. •

Note: A few activities are specifically excluded from consideration for this tax credit. These include management studies, efficiency surveys, ordinary testing and inspections, consumer surveys, and the acquisition of patents or models.

EXPENSES THAT QUALIFY

The IRS identifies several main categories of expenses that qualify for the R&D tax credit. These include:

- Salaries paid to employees working directly on the activities and their front-line managers,
- Fees paid to U.S.-based contractors,
- Legal fees paid to obtain patents, and
- Supplies used in the course of performing the R&D activities.

You can apply up to 9.1% of eligible R&D expenses as a credit against your federal income tax liability on a dollar-for-dollar basis. Plus, your state might offer a separate R&D tax credit. Many state programs mirror the federal rules that dictate which kinds of R&D activities and expenses qualify.

How to reap tax benefits from a summer vacation

If you're self-employed and planning a vacation this summer, you could reap financial benefits by combining your summer getaway with a business trip. By doing so, you may be able to claim valuable tax deductions — if you plan carefully — and help fund a portion of your summer getaway costs.

DETERMINING WHAT'S DEDUCTIBLE

From a tax standpoint, qualified trip expenses directly attributable to your business will be deductible if your trip's primary purpose is business. The key factor in determining the deductibility of trip expenses is the number of days spent on business activities compared to the number of days spent on nonbusiness pleasure activities. If more days are spent on business than pleasure, it can typically be considered primarily a business trip.

Some days you might think are pleasure days could actually be considered business days for tax purposes. For example, if you must spend an extra day away between meetings, this could be considered a business day even if you're not engaged in business-related activities that day. Plus, if adding personal days onto a business trip reduces the overall cost of the trip, you might be able to deduct certain expenses, such as lodging and meal costs (partial) for these days.

DECIDING WHAT'S REASONABLE AND NECESSARY

The following costs are generally considered to be reasonable and necessary business travel expenses. They're deductible if they are incurred during the *business* portion of your trip:

- Airfares, rail, taxi and other transportation service fares,
- Baggage handling fees,
- Car rental or other vehicle usage fees,
- Hotel, condo or other lodging costs,
- 50% of meal costs for business days, and
- Tips.

But expenses you incur on the *vacation* days of your trip generally aren't deductible. You can't deduct costs incurred by your family members on the trip either. So, for example, while you *can* deduct 50% of meal costs for yourself on the business days of your trip, you *can't* deduct your family members' meal costs on business or vacation days.

DOCUMENT, DOCUMENT, DOCUMENT

Thorough documentation of all trip activities and expenses is critical so you can easily distinguish between business and personal expenses later. This will help ensure that you claim all the deductions to which you're entitled. And you'll be able to prove your business expenses to the IRS in the event you're audited. Consult with a tax advisor for more details on your specific situation. •

This publication is distributed with the understanding that the author, publisher and distributor are not rendering legal, accounting or other professional advice or opinions on specific facts or matters, and, accordingly, assume no liability whatsoever in connection with its use. ©2017 MTCsu17

Israeloff, Trattner & Co., P.C.
CERTIFIED PUBLIC ACCOUNTANTS • FINANCIAL CONSULTANTS
1225 Franklin Avenue, Garden City, New York 11530

PRSRT STD
U.S. POSTAGE
PAID
CHICAGO, IL
PERMIT NO. 4269

Our Financial and Management Consultants Cover All Bases

Optimize your profitability and reduce your tax liability with a teammate you can trust: A leading certified public accounting, financial and management consulting firm that combines world class skills with a tradition of personal service and integrity. Israeloff, Trattner & Co. strives to optimize your financial performance with a team of dedicated professionals who can provide the ideal solution to improve your financial position. Isn't it time you made Israeloff, Trattner & Co. part of your team?

ACCOUNTING & AUDITING • MANAGEMENT CONSULTING

BUSINESS PLANNING & FORECASTING

DOMESTIC & INTERNATIONAL TAX PLANNING & COMPLIANCE

FINANCIAL & ESTATE PLANNING

MERGER & ACQUISITION CONSULTING

SUCCESSION & RETIREMENT PLANNING • WEALTH MANAGEMENT

TECHNOLOGY, HUMAN RESOURCES & MARKETING CONSULTING

Israeloff, Trattner & Co., P.C.
CERTIFIED PUBLIC ACCOUNTANTS • FINANCIAL CONSULTANTS

Offices in New York City and Garden City
1-800-945-0200
Visit us on the web at www.israeloff.com