Business Matters

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HOW TO KEEP YOUR FAMILY BUSINESS IN THE FAMILY

Family business owners often make certain assumptions — that their children will gladly succeed them or that they'll be able to transfer ownership *and* enjoy a comfortable retirement. Such assumptions can be dangerous. For starters, family members may have other career objectives. Even if they don't, succession planning can be tricky, involving both your retirement and estate plans.

DOMESTIC DRAMAS

Your first planning priority is to name a successor. If a child is active in the business and capable of taking over, confirm that he or she is interested. Then begin the grooming process. If, on the other hand, several family members are jockeying for the position, you may need to make some difficult decisions. Once you do, let everyone know your intentions well in advance of retirement. Good communication is critical to avoiding conflict.

Often, business owners don't know how they'll eventually divide their wealth among heirs who're active in the business and those who aren't. If you have significant nonbusiness assets such as real estate or a stock portfolio, you might make an equitable division by leaving those to the nonactive heirs. But if the bulk of your wealth is tied up in your business, you might give voting stock to the active heirs and nonvoting stock to the others.

FINANCING YOUR PLAN

Next consider how you'll transfer ownership and retire comfortably. You might pass on management, but retain ownership and financial control. Or, your successor might buy the business outright. Unfortunately, family business successors rarely have the cash to do so. Therefore, you might want to place the business in a trust.

A grantor retained annuity trust (GRAT) can provide you with income for a term of years and then distribute the remaining assets to your beneficiaries. Such trusts offer compelling tax advantages. When you transfer your ownership interests into the

Continued on page 4

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TO INSURE OR NOT TO INSURE

That's the LTC question

As health care costs soar and Americans live longer, long-term care (LTC) insurance is becomingly increasingly popular. If you're healthy and between the ages of 50 and 65, this may be the ideal time to buy a policy. But before you do, get the facts about the benefits — and risks — of LTC coverage.

WHAT DOES IT COVER?

LTC policies cover many care-related costs associated with debilitating health conditions. Although health insurance and Medicare generally pay for short-term care, they don't cover the expensive long-term in-patient or at-home nursing and custodial care that chronically ill or disabled patients may need to perform basic life activities such as dressing, bathing and eating.

Most LTC policies have maximum daily and lifetime benefits. Depending on the policy, it may cover only nursing-home care or pay for everything from in-home assistance to adult day care to a hospice stay. Policies also contain "elimination" or waiting periods before benefits kick in — typically between 30 and 90 days.

WHAT DOES IT COST?

LTC policies are relatively expensive, and those with higher maximums, broader care options and shorter elimination periods cost more. But your premiums generally will be lower if you buy a policy when you're younger than 65.

HYBRID MODELS

The long term care (LTC) insurance market offers a dizzying array of options, with many new products in the pipeline. One you might want to consider is a hybrid annuity / LTC insurance policy. If you don't use your premiums for LTC, they can be applied to annuity payments that will supplement your retirement income. Or, in the case of a life insurance / LTC insurance hybrid, premiums might go toward a death benefit paid out to your beneficiaries.

Other factors that contribute to the cost of LTC insurance include:

- Your current physical health and cognitive ability,
- Your family medical history,
- Whether you smoke, and
- Whether you engage in risky activities, such as piloting a small plane.

Applicants who already require LTC or have been diagnosed with such illnesses as Alzheimer's, AIDS or metastasized cancer typically don't qualify for coverage.

WHAT'S THE ALTERNATIVE?

Of course, there's always the risk that you'll pay hefty LTC insurance premiums for years and never need the benefits. For this reason, those with ample financial resources — generally a couple with at least $2.5 million in assets — might be better off paying any LTC costs out-of-pocket.

Your estate planning goals also should factor into your LTC insurance decision. Is coverage likely to preserve assets for your heirs? If so, they may be willing to pay your premiums. On the other hand, family members may be available to assume caretaker roles — in which case you might not need LTC insurance.

AN INFORMED DECISION

To ensure you make an informed decision about LTC insurance, discuss your options with your family and your financial and estate planning advisors. Your well-being and financial future depend on it. ■

SELF EMPLOYED? THERE'S A RETIREMENT PLAN JUST FOR YOU

Jason left his job — and a company-sponsored 401(k) plan — four years ago to start his own consulting business. Since then he's been too busy and too cash-strapped to save for retirement. But now his business is thriving, and he wants to know what options are available to a 45-year-old self-employed individual.

Although a Simplified Employee Pension (SEP) plan or a traditional profit-sharing plan is a possible option, Jason's financial advisor suggests a solo 401(k). Among its many benefits: Jason can contribute larger annual amounts — and make up for lost time.

BEST OF BOTH

This relatively new retirement savings option combines features of a standard 401(k) with those of a profit-sharing plan. You fund it two ways:

1. With salary deferrals — in 2012, as much as 100% of the first $17,000 ($22,500 if you are 50 or older) of your compensation, and
2. With "employer" profit-sharing contributions. If you're a sole proprietor, this can be as much as 20% of your self-employment income, subject to certain adjustment, or 25% of your W-2 compensation.

The maximum contribution limit — combining both the salary deferral and the profit-sharing contribution — in 2012 is $50,000 ($55,500 if you're 50 or older).

PLAN IN ACTION

Assuming that Jason's net self-employment income is $100,000 in 2012, he can contribute $35,587 to his solo 401(k). By contrast, his SEP contribution limit would be $18,587. However, the figures would be slightly different if Jason paid himself a $100,000 salary from his corporation. In that case, his maximum SEP contribution would be $25,000, but he could contribute as much as $42,000 to his solo 401(k) plan.

Participants can contribute larger annual amounts — and make up for lost time.

Because both SEP and solo 401(k) plans have a 2012 maximum contribution of $50,000, the solo 401(k) contribution limit advantage decreases and eventually disappears for younger participants. Those 50 and older, however, are eligible for catch-up contributions under only the solo 401(k), allowing a maximum contribution of $55,500.

ADDITIONAL FEATURES

Solo 401(k)s boast other benefits. Participants have the flexibility to contribute smaller amounts — or nothing at all — in lean years and can borrow as much as 50% of their account balance. Also, these accounts can hold nontraditional investments such as real estate. To determine whether you're eligible for participation (some small business owners with employees also may be), talk with your financial advisor. ■

GET (TAX) CREDIT FOR MAKING YOUR HOME GREENER

With the Residential Energy Efficient Property Credit, homeowners can go greener, cheaper. From now through Dec. 31, 2016, certain energy-efficient upgrades to existing homes are eligible for a 30% federal tax credit.

Qualified upgrades include the installation of:

- Solar electric property, such as solar panels,
- Solar water heaters,
- Geothermal heat pumps, and
- Small wind energy devices.

Both equipment and labor costs qualify, and there's no cap on the amount homeowners can claim. So, for example, you could install several types of energy-efficient equipment for a total cost of $30,000 and receive a $9,000 tax credit. You won't receive a refund if your credit exceeds your tax liability. But you can carry forward any excess credit to subsequent years through at least 2016, when the credit currently is scheduled to expire.

If you've been thinking about making energy upgrades to your home, the Residential Energy Efficient Property Credit provides another incentive. Just be sure you use only eligible equipment with a manufacturer's tax certification statement. Talk to your tax advisor if you aren't sure whether your energy-upgrade plans qualify.

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Continued from page 1

GRAT, it's considered a taxable gift. But the annuity you receive reduces the value of that gift. Plus, future appreciation can be removed from your taxable estate. Note one drawback: If you die before the end of the annuity period, the trust assets will be included in your estate, effectively eliminating the GRAT's estate tax benefits.

Other potential business transfer vehicles include:

Employee stock ownership plans (ESOPs). An ESOP is a qualified retirement plan that's required to invest primarily in the company's stock. It can be a tax-efficient means of transferring stock to family members and removing some equity from the business for retirement income.

Self-canceling installment notes (SCINs). A SCIN terminates a successor's purchase payment obligations on your death without adverse tax consequences. This strategy can be risky, but if you have reason to believe that you won't reach your actuarial life expectancy, a SCIN can provide your family with a tax-free windfall.

Other financing alternatives include a family limited partnership, financing the sale yourself, seeking private investment capital or even going public. Such strategies are complicated, and professional advice is essential to execute them.

TIP OF THE ICEBERG

Family and retirement income considerations are only a few of the myriad issues involved in transferring a family business to the next generation. The sooner you start planning, the better. ■