



## DYER & ASSOCIATES, P.C.

Certified Public Accountants

10415 Armory Avenue

Kensington, MD 20895

(301) 654-6200 FAX: (301) 692-1990

# Client Information Bulletin

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## Building a Foundation for a Succession Plan

### *How to transition leadership of a company*

If you are a small-business owner nearing the time when you expect to retire, you should start laying the groundwork for a smooth transition of power. Who will run the company when you leave?

Frequently, the business will have employed other family members who are logical candidates to spearhead the company when the founder steps down. Or the leadership role may be handed over to a trusted employee or group of employees. Finally, if no one emerges from within the company, you might arrange to sell the business to outsiders.

In any event, it is strongly recommended that you adopt a business succession plan, particularly if the business is staying within the family. Here are several suggestions to consider when you “hand over the reins” to other family members.

- ◆ Assemble the family and discuss your intentions with them. This is usually the best time to address any personal conflicts that could cause problems later on. In addition, you should consider the possibility of utilizing outside consultants or key employees. Perhaps you might stay on as a consultant for a short period of time.

- ◆ Designate a successor or a management group. Make it clear who will be “running the show” when you

have called it quits. Although this may force you to make some difficult choices right now, it can avoid future infighting that might ultimately destroy your business. Make sure the other key employees will remain on board.

- ◆ Secure adequate life insurance for yourself and other key executives. The proceeds from a life insurance policy can be used to pay for estate taxes if the owner should suddenly die.

- ◆ Execute a buy-sell agreement. This agreement typically spells out the terms for a buyout of the owner's interest upon his or her death, disability or retirement. For example, it may cover the valuation of the business, the source of proceeds for the buyout and various other provisions. However, this valuation is not necessarily binding for estate-tax purposes.

- ◆ Have a “power of attorney” drafted. This legally binding document may be used to keep the business operating if the owner is unexpectedly incapacitated. It names the person to take over in the event this occurs.

- ◆ Consider the potential impact of estate taxes. For instance, the succession plan can provide for the payment of estate taxes to effectively be spread out over 15 years when a closely held business is involved.

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◆ Tie up all the loose ends. The plan should provide guidelines for any other unusual circumstances or specifics relating to your particular profession or industry.

Generally speaking, the sooner you begin to draw up a business plan, the better. After all, it is important to provide for contingencies. Don't put this process off indefinitely.

## Five Steps to Take Before Switching Jobs

### Financial considerations include fringe benefits

After years working at one company, you have been offered a promising position with a different employer. Should you make the switch? Of course, salary is a significant factor, but there is a lot more at stake with this life-altering decision.

The following are five steps you can take before you commit to a change.

**1. Review your retirement plan options.** Assuming you have a qualified retirement plan at your current position, you will be faced with several intriguing choices if you leave. In general, the vested benefits are portable or can be accessed upon termination of employment. Specifically, you might

- ◆ Roll over a lump-sum distribution to the new employer's plan or an IRA. With a trustee-to-trustee rollover, there is no income tax withholding on the distribution.
- ◆ Leave the funds in the plan. The amounts are subject to the usual rules for withdrawals (e.g., distributions prior to age 59½ are generally subject to a 10% penalty tax in addition to regular income tax).
- ◆ Take distributions in cash, and pay the resulting income tax plus any penalties.

**2. Protect pension plan assets.** If you are entitled to a pension, you may not have access to the funds until you

retire, even when you switch to a different job. Other plans may permit distributions of vested benefits. Consider all the implications.

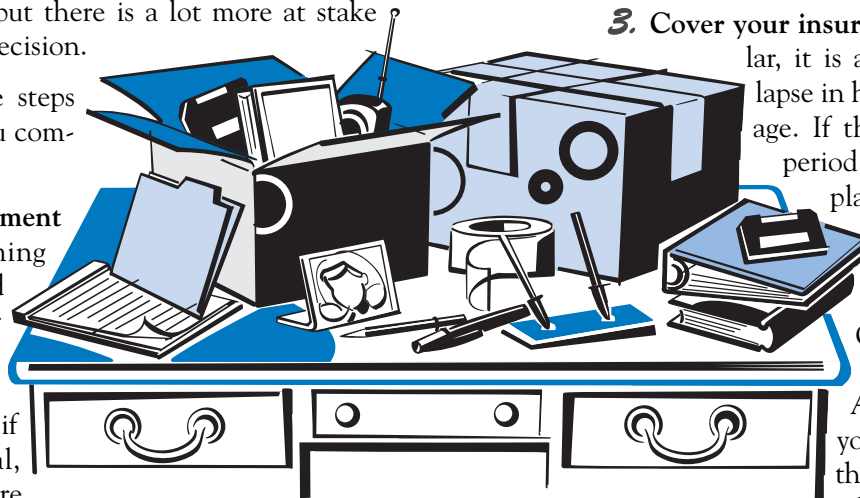
**3. Cover your insurance bases.** In particular, it is advisable to avoid any lapse in health insurance coverage. If there will be a waiting period with a new employer's plan, you can continue coverage from your old employer through COBRA (short for the Consolidated Omnibus Budget Reconciliation Act). Under COBRA, you usually have to pay the entire premium yourself, but it could be well

worth the peace of mind. Similarly, see how other insurance benefits will be affected.

**4. Evaluate stock options and grants.** A stock option enables you to buy company stock at a specified price while a grant allows you to receive stock at no charge. Determine the value of grants and stocks. If you will be leaving a sizeable amount of money on the table, you may want to reconsider the job switch or negotiate comparable benefits from your new employer. Consult with a tax expert regarding the exercise of stock options.

**5. Check your FSA status.** With a flexible spending account (FSA), you contribute to an account to pay health care or dependent care expenses on a pretax basis. When you leave the company, you must forfeit any unused funds in your FSA. On the flip side, the employer generally bears the burden for expenses if you have already collected on claims that have exceeded your payroll contributions.

Finally, take a close look at the "big picture," considering the benefits offered at each position. This will help you make an informed decision based on all the relevant factors.



### Give Us A Call!

Do you have any questions or comments about this newsletter or your individual situation? Please do not hesitate to contact our office.

We would be glad to serve you in any way we can.

# Protecting Your Business: Use a Computer Firewall

## Set up a system that restricts data traffic

**Y**our company's proprietary information is its lifeblood. So you cannot run the risk in this high-tech world that unscrupulous hackers might gain access to your vital computer data. If you have not yet installed an adequate firewall on your network, there is no time to delay.

What exactly is a firewall? Simply put, it is a software program or hardware device that filters the data coming through Internet connections into your company's computer network. If the data sets off the firewall's alarms, it will not be allowed through.

For example, say that your company employs more than 100 workers, so it has literally dozens of computers interconnected on the network. The company may be connected to the Internet through a T1 or T3 line. If you do not have a firewall in place, all of the company's computers are at risk from someone else on the Internet.

A knowledgeable hacker could probe those computers by trying to make FTP connections or telnet connections to them. If one of your employees unintentionally creates a security opening, an outsider could conceivably exploit the "hole" in the system.

Conversely, a firewall dramatically changes this state of affairs. For instance, if you establish a firewall at every Internet connection through a T1 line coming into the network, it is able to implement specific security rules. One possibility is to limit the number of computers able to receive FTP traffic. Similarly, your company can implement comparable security measures for FTP servers, Web servers and so on.

Furthermore, a firewall enables a company to establish a methodology for connecting to Web sites and transmitting files over the network. To summarize, the firewall provides you with control over how and when employees use the computer network.

Firewalls generally are based on one of following three methods for controlling information flow on the network.

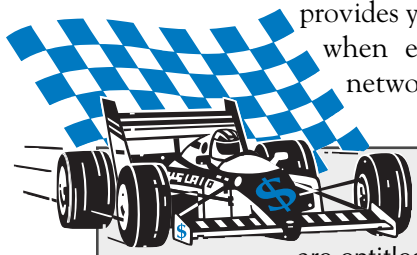
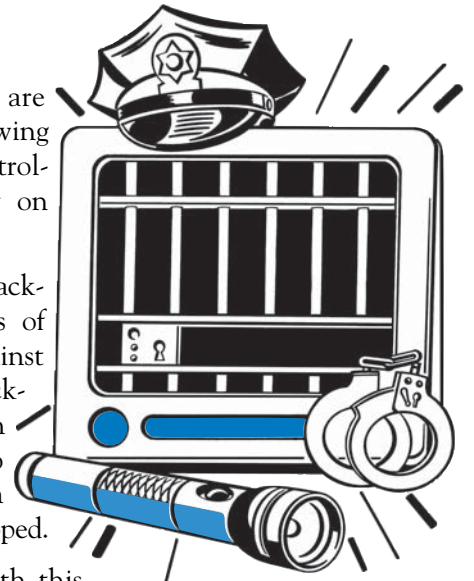
**1. Packet filtering:** Packets (i.e., small groups of data) are analyzed against a set of filters. The packets that pass through the filters are sent to the requesting system while all others are stopped.

**2. Proxy service:** With this method, Internet data is retrieved by the firewall. Then it is delivered to the requesting system and vice versa.

**3. Stateful inspection:** This is a relatively new firewall method. Instead of inspecting the contents of the packets, it compares certain elements with a database of trusted information. Information traveling from inside the firewall to the outside is monitored for specific characteristics. If a comparison of those characteristics results in a reasonable match, the data is transmitted. Otherwise, the firewall stops the flow of information.

Be aware that firewalls are customizable. This means that you can add or remove filters based on several conditions. Some of these conditions are IP addresses, domain names, protocols, ports or specific words or phrases. As an example, your company might set up only one or two machines to handle a specific protocol and ban that protocol on all other computers.

*If you are not particularly computer-savvy, lean on the technical experts within your company or outside consultants. This is simply too important to leave to chance.*



### Speeding Up Refunds of Estimated Tax

Did your calendar-year company overpay its estimated tax liability for 2007? Of course, you are entitled to a refund for the overpayment. Best of all, you don't have to wait for it very long.

**Here's why:** If you file the appropriate paperwork with the IRS, you can obtain a fast refund from the federal government. In fact, your company should receive the refund within 45 days of the application. This special refund procedure is available only if the overpayment exceeds the estimate by at least 10% and amounts to \$500 or more.

The deadline for applying for fast refunds for the 2007 tax year is March 17, 2008, but you don't have to wait until then. Consult with your professional tax return preparer.

# How to Identify Miscellaneous Expense Deductions

## *Two main categories of deductible expenses*

**M**ost income tax deductions, such as charitable donations or medical expenses, have their own “identity.” But there is a collection of deductible expenses that do not fall into a clearly defined category. The IRS refers to them as miscellaneous itemized expenses.

**Background:** Miscellaneous expenses are generally not big-ticket items—although there are several key exceptions—but they can add up to a sizeable deduction at tax return time. There is, however, one catch: Your annual deduction is limited to the excess above 2% of your AGI for the year.

For instance, suppose that your AGI for 2007 is \$100,000 and you have incurred \$1,500 of miscellaneous expenses during the year. In that case, your deduction is zero. On the other hand, if you have \$2,500 in miscellaneous expenses, you can deduct \$500.

Generally, miscellaneous expenses are attributable to one of two main categories:

**1. Production-of-income expenses:** This group includes expenses related to the production of income through investments, financial planning, retirement planning and tax assistance. Although this list is not all-inclusive, some common examples are safe-deposit rentals to store non-tax-exempt securities; accounting fees and legal fees to produce or preserve income; custodial fees for income-producing property and IRAs; fees paid to collect inter-

est or dividends; hobby expenses (up to the amount of hobby income); fees for investment and tax counsel; appraisal fees for charitable contributions and casualty losses; and the cost of services, periodicals, manuals and other materials related to tax assistance.



Note that the cost of having your tax return prepared by a professional is deductible as a miscellaneous expense.

**2. Employee business expenses:** The other main group of miscellaneous expenses consists of unreimbursed employee business expenses. It includes such expenses as dues paid to professional societies; union dues; employment-related education; malpractice-insurance premiums; qualified home-office expenses; subscriptions to professional journals and magazines; work clothes or uniforms; cellular phones and home computers (when required as a condition of employment) and qualified travel and entertainment expenses (but only 50% of entertainment costs are eligible for the deduction).

Furthermore, the cost of seeking employment (e.g., agency fees) is deductible as a miscellaneous expense, even if you don't end up with the job.

*As is usually the case with taxes, there are several exceptions to these general rules, so be sure to obtain expert tax assistance.*

## Facts and Figures

### *Timely points of particular interest*

➔**Reasonable Compensation**—In a new case, a dynamic company founder received a relatively low salary for several years so the business could expand. Under his leadership, the company prospered. When the owner was later rewarded with a \$2 million package, the IRS objected. But the Tax Court found the compensation to be “reasonable” and approved the company's deduction. **Note:** Currently, it may be preferable for small-business owners to receive dividends qualifying for a reduced tax rate.

➔**Reviewing Performance**—Business managers carefully evaluate job candidates before they are hired. But then the process usually stops even though it is just as important to review work performance once the employees are on board. Continue to monitor such characteristics as competence, judgment, energy focus, relationship skills and trust. When it is warranted, provide constructive criticism to members of the workforce, particularly the new-hires.

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