GS Blog Round-Up

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Art collectors should use tax laws to protect heirs

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With proper plan–ning, collectors can enhance the financial benefits of their art collection. If you are a serious art collector, you should be aware of the numerous tax issues related to the ownership and transfer of art and collectibles. Following is a discussion of some of the more relevant tax issues and related tax planning strategies:

Estate and gift tax concerns

Because art can be amongst the most highly appreciating assets in a collector's estate, wealthy collectors who wish to minimize their gift and estate tax liabilities should consider developing and executing a lifetime gifting strategy. One effective strategy is to use the $14,000 annual exemption in conjunction with valuation discounts by gifting fractional interests in art.

For example, if a husband and wife have two children, they may gift a total of $56,000 each year in cash or property to their children without any gift tax implications (each parent gifts each child $14,000). When gift–ing fractional interests in property, discounts for lack of control of the property and lack of marketability of the partial interest can be taken. Assuming a 30 percent total valuation discount, the husband and wife in this example could gift fractional interests in art with a pre-discounted value of $80,000 a year without gift tax implications. Not only does this remove gifted art from the parents' estate tax free, it also removes future appreciation of the art from their estate.

Currently, an individual could make $5,450,000 in total gifts during his or her lifetime without paying gift tax. Any lifetime gifts exceeding this total would be taxed at 40 percent.

It is also important for wealthy collectors to consider the financial and tax ramifications of holding a significant art collection with the hope of passing it on largely intact to their heirs. A large estate that does not have enough liquid assets to sufficiently pay its estate taxes might put the heirs in the position of having to sell valuable works of art on short notice for a fraction of their value.

Reducing taxes related to unreported transfers

Collectors may find themselves in possession of art that was trans–ferred to them from a previous generation without being disclosed properly on the appropriate gift or estate tax returns. Here is a typical scenario: John Smith purchased a painting several decades ago. When John died, his son simply took the

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painting off the wall and put it in his home. The painting was worth $100,000 when John died. Since John had a large estate, this painting would have been subject to estate tax. The transfer was not reported either because the son wasn't aware of the reporting requirement or because he felt the transfer would go unnoticed by the taxing authorities (i.e. it would pass "below the radar screen"). Several years after John's death, the son would like to sell the painting which is now valued at more than a million dollars.

Depending on the specific circumstances, there are various strategies a collector may utilize to help mitigate their tax exposure...

A sale of that magnitude to an unrelated party would no longer fall "below the radar screen". The sale would almost certainly be reported to the IRS, which would most likely scrutinize the transaction. If the IRS were to find the son acquired the property by inheritance from his father and the father's estate should have paid estate tax on this painting, the unpaid estate tax would have to be paid by the son, along with inter–est and substantial penalties. No matter how many years passed between John's death and the sale by the son, if the omission is determined to be due to fraud (intentional omission), the statute of limitations would not have run out since there is no statute of limitations with respect to fraud.

Depending on the specific circumstances, there are various strategies a collector may utilize to help mitigate their tax exposure in this situation.

Charitable contributions

Some popular strategies for charitable giving include:

- Outright donation to a qualified charity – Collectors who are not dealers can receive a tax deduction equal to the fair market value of art donated to a qualified charity. In addition, the excess of the fair market value of the art over its cost to the collector does not have to be reported as income by the collector when the art is donated.
    - If a collector donates art with a fair market value which is sig–nificantly higher than his or her cost, the decrease in income tax resulting from the tax deduction for the donation may be greater than the amount of net cash realized from selling the art, after de–ducting selling expenses and income tax on the gain recognized. In this instance, it is more profitable for the collector to donate the art than to sell it.
    - This is also a good strategy for collectors who have incomplete records of the cost basis of art since the deduction is based on the fair value of the art and the cost basis becomes irrelevant.
- Donation of an undivided portion of an interest – A popular way of executing this type of strategy is for a collector to donate to a museum the right to take possession of a work of art for a specified period each year. This works particularly well for a collector who spends a certain part of each year away from a residence which houses art. For example, a collector who spends winters in Flori-

da and lives in New York the rest of the year could donate to a museum the right to take possession of a work of art from his New York residence during the winter. This commitment to the museum must be permanent. The collector would benefit from the arrangement as follows:

- The collector establishes goodwill and philanthropic capital with the museum and within the community.
- The collector retains the art during the period he lives in hi New York residence.
- The collector receives an income tax deduction in the initial year of the donation equal to the fair market value of the art multiplied by the percentage of the year the art is given to the museum.
- The collector doesn't have to worry about the maintenance of the art during his time away from the New York residence.

There are strict requirements that need to be met in order for a donation of an undivided portion of an interest in a work of art to be held valid under Federal law. Collectors should consult with a tax professional experienced in this area when entering into this type of arrangement.

This article has addressed only a few of the relevant tax issues and related tax planning strategies collectors should consider in developing a tax and finan–cial plan for their collections.

Collectors should work closely with an experienced financial and tax advisor to develop a plan that meets all of their needs.

Art collectors should use tax laws to protect heirs

Effective Marketing On a Budget

Does your professional services firm have a minimal marketing budget or lack in-house marketing staff? Are some of your competitors outspending you 2, 5 or even 10 to 1? Under such circumstances, attracting new business may seem like an impossible goal.

But professional service firms with small budgets can market themselves effectively and build their clientele with many low-cost (sometimes even free) marketing options allowing you to stretch your funds.

Relationships and Customer Service

We've heard it a million times, that relationships and good customer service will increase your business development efforts. Even though this is a simple concept, many organizations do not have clearly mapped out training and processes to assist in this endeavor. Start by creating a reference guide for employees of what is expected of them by way of customer service and relationship building. Examples include: return phone calls within a certain amount of hours, give progress updates before they are requested, be well versed in the firm or company service offerings. These activities, although simple, go a long way in developing trusting relationships with your clients.

Satisfied clients are your best source for new business, so be sure to check in with them at least every three to six months. Although phone calls are acceptable, face-to-face meetings and the informal conversations are much better. Invite your best clients to non-billable activities such as lunch or a social event where you can have a good chat.

Similarly, cultivate non-client referral sources such as other service professionals serving the same group of clients. Remember that referrals are a two-way street: Your best leads will likely come from professionals to whom you've referred business.

Also, encourage those suited in your firm to attend conferences and other business, professional and industry events as time permits. Simply by talking with other participants in your niche, service or industry you can increase awareness of your firm and start relationships that result in referrals or engagements. As an example: A new manager in my firm recently received a referral from someone she had only met once because she attended an event and spoke to this person about what she did and where her practice was located. Even though she didn't know the person well, he referred her because she came across as credible and our firm was in the right location for the referral. If she would not have attended the event, she would not have received the referral.

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Agree On Who You Are as a Firm

Be sure to train ALL of your employees on effective ways to communicate your brand. As simple as it sounds, the key to successful branding is repetition, repetition, repetition.

Without the resources of hiring a branding consultant, you need to understand who you are as a firm and how you want to position yourself to the public. This will allow your staff to better articulate one focused message. Brainstorm ideas about what your firm does well, (for example, keeps costs down or boasts a high rate of clients in a certain industry) and how it differentiates you from similar firms.

Once you've established a brand "identity," deploy it at every opportunity and in all possible formats. Establish talking points for meetings with prospective clients, informal chats with referral sources and speeches to community groups. Include key messages in your marketing collateral, on the home page of your website and in advertisements and paid sponsorship spaces.

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Competing with the Big Guys

In many ways, the Web provides a level playing field where dedication and enthusiasm counts more than money. Although you should not skimp on building an attractive, easy-to-navigate and search-engine-optimized (SEO) website, a staff member can be responsible for updating your site. Social media platforms like LinkedIn, Twitter, Facebook, and Google + — probably the most effective communication tools available online — cost nothing to use.

If you don't have a blog, consider starting one using a free platform such as Blogger or WordPress. The Web arguably has a glut of blogs, but there's always room for one more that addresses a specialized niche or provides insights on current issues in an engaging voice. Blogs are a great way to communicate with clients and prospective clients in real time. They also help to feature established and up-and-company employees.

And don't forget to participate in online forums related to your area of expertise (keeping in mind the forum's rules about business solicitation).

Get Creative

Although you'd probably prefer a more robust budget, it's possible to build your clientele on a shoestring if you stay creative with your ideas, prioritize expenditures and take advantage of low-cost marketing strategies.

Large Changes to Overtime Rules Handed Down by DOL

The U.S. Department of Labor (DOL) has made dramatic changes to the determination of which executive, administrative and professional employees — otherwise known as "white-collar workers" — are entitled to overtime pay under the Fair Labor Standards Act (FLSA). The new rules will make it more difficult for employers to classify employees as exempt from overtime requirements. In fact, the DOL estimates the changes will make an additional 4.1 million salaried workers eligible for overtime pay when they work more than 40 hours in a week.

The current rules had not been revised since 2004, prompting President Obama to call for the updates. The DOL issued a proposed rule in July 2015 and received more than 270,000 comments in response. The final version of the new rules will become effective December 1, 2016.

By the GS Tax Department

Requirements for white-collar exemptions

To qualify for a white-collar exemption from the overtime requirements, an employee generally must satisfy three tests as follows:

	Old Rule (Current)	New Rule (effective December 1, 2016)
Salary Basis Test	The employee is salaried, meaning he or she is paid a predetermined and fixed salary that's not subject to reduction because of quality or quantity of work performed.	No Change to Salary Basis Test
Salary Level Test	The employee is paid at least $455 per week or $23,660 annually.	The employee is paid at least $913 per week or $47,476 annually. Up to 10% of the salary can be met by non-discretionary bonuses, incentive pay, and commissions, as long as paid at least quarterly.
Duties Test	The employee primarily performs executive, administrative or professional duties. Relaxed duties test for certain highly compensated employees (HCEs) with total annual compensation of at least $100,000, including a salary of at least $455 per week.	No Change to Duties Test Relaxed duties test for certain highly compensated employees (HCEs) with total annual compensation of at least $134,004, including a salary of at least $913 per week.

The revisions in the final rule mainly relate to the salary level test. The rule increases the salary threshold for exempt employees to the 40th percentile of weekly earnings for full-time salaried workers in the lowest-wage Census region...

Certain employees (for example, generally doctors, teachers and lawyers) are not subject to either the salary basis or salary level tests.

Significant changes under the final rule

The revisions in the final rule mainly relate to the salary level test. The rule increases the salary threshold for exempt employees to the 40th percentile of weekly earnings for full-time salaried workers in the lowest-wage Census region (currently the South) — $913 per week or $47,476 per year.

In response to what the DOL described as "robust comments" from the business community, the final rule allows up to 10% of the salary threshold for non- highly compensated employees to be met by nondiscretionary bonuses, incentive pay and commissions, as long as these payments are made on at least a quarterly basis. Thus, an employee's production or performance bonuses could now push him or her over the threshold and into exempt status (assuming the other tests are satisfied).

The rule also updates the HCE threshold above which the relaxed duties test applies. It raises the level to the 90th percentile of full-time salaried workers nationally, or $134,004 per year.

The final rule continues the requirement that HCEs receive at least the full standard salary amount — or $913 — per week on a salary or fee basis without regard to the payment of nondiscretionary bonuses and incentive payments.

The standard salary and HCE annual compensation levels will automatically update every three years to maintain the levels at the prescribed percentiles, beginning January 1, 2020. The DOL will post new salary levels 150 days before their effective date.

The duties test

The final rule makes no changes to the duties test. In the proposed rule, the DOL had sought comments regarding the effectiveness of the test at screening out workers who aren't bona fide white-collar workers.

But it determined that the new standard salary level and automatic updating will work with the duties test to distinguish between overtime-eligible workers and those who may be exempt. Moreover, as a result of the revised salary level, employers won't need to consider the duties test as often — if a worker's pay doesn't satisfy the salary level test for exemption, the employer needn't bother assessing the worker's duties.

Compliance options

According to the DOL, employers have a range of options when it comes to complying with the changes to the salary level. Options include:

Doing nothing. You might choose to do nothing if your white-collar workers fall short of the new salary level but never work more than 40 hours per workweek.

Raising salaries. You may want to raise the salaries of employees who meet the duties test, have salary near the new salary level and regularly work overtime. Paying them at or above the salary threshold will maintain their exempt status.

Paying overtime above a salary. You could continue to pay employees a salary covering a fixed number of hours, which could include hours above 40. For example, you might:

- Pay employees a salary for the first 40 hours of work per week and overtime for any hours over 40.
- Pay a straight-time salary for more than 40 hours in a week for employees who regularly work more than 40 hours, and pay overtime in addition to the salary. You will only be required to pay an additional half-time overtime premium for overtime hours already included within the salary, plus time and a half for hours beyond those included.
- Agree with the employee on a fixed salary for a workweek of more than 40 hours, with the salary including overtime compensation under certain conditions. Employees must always be paid based on the hours actually worked during the workweek, though, so salary adjustments may be necessary at times. This will likely work best for employees who consistently work the same amount of overtime every week.
- For employees with fluctuating hours, pay a fixed salary covering a fluctuating number of hours at straight time if certain conditions are met.

And, of course, you might reorganize workload distributions or adjust employee schedules to redistribute work hours in excess of 40 across current staff. You could also hire additional employees to reduce or eliminate overtime hours worked by your current staff.

The big picture

The cost of the new overtime rules is more than just the increased compensation; it also includes additional payroll tax liability on that compensation, as well as administrative costs to comply. We can help you come into compliance with the new DOL overtime rule and determine the overall impact on your bottom line.

Choosing the Cash or Accrual Method of Accounting for Your New Business

By GS Editor

When you start a business, you have many decisions to make. One very important decision is the method of accounting your business will use for reporting income and expenses on your tax return. The two methods most commonly used are *Cash* and *Accrual*.

CASH METHOD

The cash method is the easiest to implement, and is also the most commonly used. Under the cash method of accounting, you recognize income when you receive a payment from a customer and you take a deduction when you pay qualifying expenses. If you perform services but do not receive the payment until the next tax year, that payment is not considered income until received in that next tax year.

The cash method closely reflects your cash flow — how money is coming in and out of your business. The drawback is that your records may not help you track how much people owe you or how much debt your business owes.

ACCRUAL METHOD

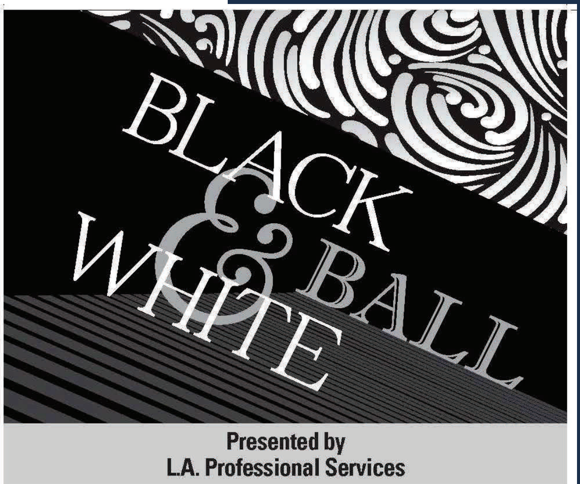
If you choose the accrual method, you recognize income when you render services or sell your products, even if you do not expect to receive payment for several months. The money your customers owe you is your "accounts receivable." On the expense side, if you buy something today and pay for it later, you deduct the cost now. What you owe for purchases you've made is your "accounts payable."

The accrual method better reflects how your business is actually doing because you can match income and expenses in the proper period.

As a new business owner, you will want to consider the pros and cons of each method before deciding which is best for your business. The nature of your business may require that you use the accrual method, though most small businesses with sales under $5 million per year can choose either method. Businesses with inventory would typically use the accrual method.

Once you commit to a method, if you later want to change to a different method, you may need to get approval from the IRS to do so. Speak with your accountant before deciding the method that will be best for your new business.

Michael Savoy Honored by National Jewish Health and Los Angeles Professional Services



Michael Savoy, CPA, CGMA, a senior shareholder at Gumbiner Savett Inc., is being honored with the Humanitarian Award at the National Jewish Health and Los Angeles Professional Services Black and White Ball to be held on June 4, at the Skirball Cultural Center, in West Los Angeles.

The Humanitarian Award recognizes an honoree who has contributed greatly, both through civic and charitable benefaction, and who is a distinguished leader in their field. “I am very excited and proud that Michael is receiving this incredible honor” stated Valerie Colin, a shareholder at Gumbiner Savett Inc., “I have known Michael for almost 40 years and he embodies all of the qualities that this award salutes.” This honor follows Savoy’s many years of continued leadership in the accounting profession, and his dedication to the community. Savoy has demonstrated his commitment to the community through his work with numerous charitable organizations. Savoy is a former board member of a privately held, not-for-profit, day school in Northridge and served as treasurer of the school for 6 years.

Aside from his charitable endeavors, Savoy has proven himself as a dedicated leader in the accounting and business field time and time again. He is a past president and is currently on the board of the California Board of Accountancy. Savoy also serves on the board of the Los Angeles Chamber of Commerce as their Treasurer. He is a member of the American Institute of Certified Public Accountants (AICPA), the California Society of Certified Public Accountants (CalCPA), and the Employee Stock Ownership Plan Association.

By GS Editor

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