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Business Owner's Perspectives

Trends and Strategies for Owners of Closely Held and Family Businesses

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Tax Topics

Remote Work May Cause Multistate Tax Issues

It used to be that employers knew where their employees worked—in the office every day. But in another unexpected fallout from the pandemic, the answer to "Where do you work?" is strangely unclear for many teleworking employees and their employers.

Employees may work in the same state as they did before the pandemic, but it's just as likely that they've been working elsewhere, at least temporarily—at the beach, in the mountains, halfway across the country, or in a different country altogether.

The reason this matters is, of course, taxes. Teleworking employees may create state and local tax (SALT) liabilities depending on where they earn their compensation and for how many days per year they work in a different state than their employer.

An Overview

Generally, a state taxes income earned in its state. If an employee works outside the state where his or her employer is located, there is a chance he or she could be subject to income taxation by both states.

During the pandemic, many states offered temporary relief to taxpayers to avoid this scenario, and many issued guidance on pandemic-related remote work arrangements relative to which state—the employer's location or the employee's location—would collect income tax.

Also, some states have "convenience-of-the-employer" rules, which allow employers to treat out-of-state compensation as if it were earned at the employer's location. (See "Income Tax" section below.)

States that have lost tax revenue due to the pandemic are eager to recoup what they can. Taxing out-of-state workers is one way to potentially make up for lost revenues, and now that declared states of emergency are largely past, the compliance grace period for SALT is ending.

Income Tax

While many companies had systems in place pre-pandemic to track traveling employees' days in various locales, few were concerned with where the rest of their employees worked. COVID changed that. Living and working in two tax jurisdictions means that employers and employees must pay attention to resident and nonresident income tax withholding rules.

For people working as "nonresidents" in a state, income tax withholding is required only on the wages earned in that state. However, the convenience-of-the-employer rule—which assumes the employee is working out of state for the convenience of the employer—means that some states will tax income not earned in the state. This "double taxation" is often offset by a tax credit in one state or the other, but that is not always the case.

It may take states some time to reach a final resolution about this withholding issue relative to COVID. For example, employees had no option but to work remotely in response to "stay-at-home" mandates, so where does convenience of the employer enter the discussion? In most cases, this issue is still unresolved.

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Word to the Wise

Take Advantage of Low Interest Rates

They say nothing lasts forever, and low interest rates are no exception. There's a lot a business owner can do with such preferable rates, so consider how your business and family might benefit. Here are some ideas to consider.

Borrow from the company: Assuming your company is in good financial shape, think about borrowing from it. If you borrow from your company, it's considered a private loan. The applicable federal rate (AFR), published by the IRS, is the minimum interest rate allowed for such loans. (This rate also applies to loans between family members.)

At the time of this writing, applicable federal rate for short-term loans (up to three years) is less than 0.2 percent. For mid-term loans (from three to nine years), the rate is less than 1 percent, and for long-term loans (more than 9 years), the rate is less than 2 percent. Who wouldn't be happy with terms like these?

Similarly, you could personally lend a child or other family member money at the AFR, and he or she could invest it in something earning a much higher rate of return. An added benefit of this arrangement is that it gets cash out of your estate while incurring very low interest costs for the child or other relative.

Remember that you must properly document these types of loans and charge at least the AFR to avoid IRS scrutiny.

Consolidate for refinancing: Now is a good time to look at real estate, major projects, expansions, and renovations. Yes, material costs are high right now, and material supply chains are clogged. But with interest rates so low, refinancing could be a wise move and deliver increased cash flow and flexibility.

Also, consider buying what you're now leasing. Unlike residential real estate, the cost of office space has remained stable. With so many people working from home, it's likely that an office space glut will remain, and there may be bargains in your area. (Note that industrial and commercial space has not followed this pattern. In fact, it's become more expensive as companies are onshoring more due to pandemic-related supply chain disruptions.)

Work on your estate plan: Preserving your wealth for your family is always worthy of attention, but some estate planning options are especially attractive when interest rates are low.

For example, a charitable lead trust (CLT) is a gift of cash or other property to an irrevocable trust. A named charity receives the income stream from the trust for a defined number of years. In the meantime, depending on how the trust is structured, the donor gets a current income, gift, or estate tax deduction on the donated assets. Once the income stream period ends, the remaining assets are distributed to non-charitable beneficiaries, such as family members.

This type of trust works well in a low-interest rate environment because IRC Section 7520 rates are prescribed as the rates used to value the charitable lead and remainder interests. The lower the federal rate, the higher the income or gift tax deduction.

Some donors create CLTs in conjunction with a donor-advised fund named as the lead beneficiary. This arrangement enables the donor to strategize and influence the nature of the charitable giving during his or her life and after death.

Make Your Money Work

Use your assets wisely. No one knows how long interest rates will remain low, and you may discover great opportunities to borrow, refinance, and plan to your advantage.

Let us help you brainstorm ideas to make your money work best for you, your family, and your company.

Teleworking Tips

How to Succeed in the New Work Environment

When it comes to corporate culture, employees highly value flexibility. In fact, flexible work arrangements are a competitive advantage for many companies seeking to hire top talent.

Some businesses were comfortable with flexible work schedules and teleworking long before the pandemic. Others were forced into flexibility, and many have been pleasantly surprised at the upside of the "new" work environment.

What are some of the benefits your company has reaped from a more flexible workplace? Is your company planning for a flexible future? If so, here are some tips to make it work:

Formalize. It's hard to plan your space needs when you don't know how many people will be in the office. If you're going to offer remote work arrangements, create a list of acceptable options.

For example, some companies have mandated several days of overlap for all employees every week. Others have asked their employees to standardize a weekly schedule of days in and out of the office.

It's up to your executive team to decide what to offer, but whatever the arrangements, put them in writing and ask employees to sign an agreement to be where they say they'll be during the workday.

Support. Robust IT support is a must for companies with teleworking employees. Depending on the sophistication of your employees' technology needs, your IT team may want to consider quarterly audits and cybersecurity (re)training to be sure everyone's remote setup is high functioning and secure.

Just as important is another form of support—support for managers who are managing remote workers. Some managers have had difficulty measuring productivity or have been frustrated by employees not being as accessible as they would be in the office. Addressing these issues—and expectations—are excellent topics for manager training.

Communicate. Having an in-and-out or largely remote workforce means there's less impromptu "water cooler" interaction among employees. Many workers miss this casual type of conversation and the opportunity to discuss ideas with colleagues on the fly.

Having town hall-style meetings once a month, lunch-and-learns by video call, and scheduled team catch-ups can make up for a lack of in-person exchange and collaboration. If you're making changes, whether to policies or personnel, overcommunicate them. Use every channel—email, phone, and messaging—recognizing that everyone has different communication preferences.

Also, holding regularly scheduled all-hands video or in-person meetings is an easy way for employees to hear from the executive team about new initiatives. Put it on the calendar for the same time each month so your team comes to expect it.

Engage. How can you build camaraderie when people aren't in the office? Easy! There's no reason why you can't encourage employee volunteer opportunities and after-work social gatherings. As in pre-pandemic days, people are typically eager to gather for sporting or charity events, an after-work social, or holiday party.

Many of our clients have adopted flexible schedules for their workers. We're happy to share best practices with you.

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Nexus

Another sticky issue for employers with remote workers involves sales and income tax nexus—the connection a business has with a state or taxing jurisdiction.

If a business has no presence in a state other than an employee teleworking from there due to the pandemic, does the employee's home office create nexus?

Several states have issued guidance indicating that an employee's home office doesn't create nexus "during the duration of the [COVID] emergency" but haven't weighed in about what happens post-emergency. Also, different states have different rulings, and no federal legislation has passed that would address state inconsistencies, despite several bills having been drafted over the past 10 years.

Pay Attention

With remote working becoming a way of life, a lack of uniformity among states will potentially mean bigger compliance burdens for employers and bigger tax filing burdens for employees. SALT liabilities can be complicated—and expensive—so be sure to get sound advice from your trusted tax advisor.

Our SALT team is ready to assist you in sorting out your tax and nexus issues. Contact us today to set up a time to talk.

When Do You Need a Forensic Accountant?

Fraud happens—even at careful companies. It typically comes to light during a valuation, litigation, divorce, audit, or insurance renewal. But sometimes an owner or executive will simply notice that something is "off" with the financials and can't figure out why.

Forensic accountants are specially trained to examine financial records. Using a combination of accounting, auditing, and investigative skills, forensic accountants uncover financial crimes such as fraud, embezzlement, or corruption and can provide litigation support by testifying in court as an expert witness.

To prove their expertise, some CPAs earn the Certified in Financial Forensics (CFF) credential from the American Institute of Certified Public Accountants or the Certified Fraud Examiner (CFE) credential from the Association of Certified Fraud Examiners.

Forensic accountants use a variety of techniques, including:

Bank account analysis: If the business is cash heavy, looking at the company's bank accounts can reveal details about the company's funds and cash flows. Do deposits accurately reflect receipts, loans, insurance proceeds, and other payments? If not, where is the missing money? Are other bank accounts being used to hide assets?

Fraud investigation: If an employee is embezzling or misappropriating business assets, a forensic accountant can examine internal documents to uncover fictitious accounts, contracts, invoices, kickbacks, ghost employees, fake vendors, personal expenses, and fraudulent expense reimbursements.

Inventory assessment: Missing inventory is a clue to misappropriation or billing schemes, and understating inventory and cost of goods can make a company appear more profitable. Forensic accountants can determine how inventory is tracked and accounted for and illuminate discrepancies.

Damage calculation: Because forensic accountants also calculate business damages, they are helpful in breach of contract, product liability, construction, and intellectual property claims.

If you are concerned about potential fraud at your company, hiring a forensic accountant can help you uncover the truth.