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The ABCs of RMDs

You *may* begin taking penalty-free retirement plan distributions as soon as you turn 59½. But, after you turn age 70½, you *must* begin taking required minimum distributions (RMDs) from your employer-sponsored defined contribution plans and traditional IRAs. If you don't, the consequences are severe: The penalty on any shortfall — that is, the difference between what you should have taken and what you actually took — is 50%.

RMD rules

RMD rules apply to 401(k), 403(b) and 457(b) plans, SIMPLEs and traditional IRAs, including Simplified Employee Pension (SEP) plans. The regulations don't apply to Roth IRAs if you're the original owner of the account. You can avoid the RMD rule for a Roth 401(k), Roth 403(b) or Roth 457(b) by rolling the funds into a Roth IRA.

RMD rules apply to 401(k), 403(b) and 457(b) plans, SIMPLEs and traditional IRAs, including Simplified Employee Pension (SEP) plans.

To calculate the minimum amount you must take from your retirement accounts each year, you divide your balance at the end of the previous tax year by the applicable IRS divisor. Your RMD will vary with the balance in the account, your age and possibly your spouse's age.

If your retirement funds are spread across multiple accounts, you'll need to figure out your RMD based on the balance in each. So, for example, if you have three IRA accounts with $25,000 in each, your RMD must include all three balances. You can take the distribution from any or all of the IRA accounts, as long as the amount is at least equal to the RMD. However, RMDs from other accounts, such as 401(k) plans, are determined separately.

Finally, don't forget that your RMDs generally will be taxed for the simple reason that the funds have been saved through tax-deferred accounts. However, to the extent that a distribution is a return of basis (which may occur, for example, if you make nondeductible contributions to a traditional IRA) or is a qualified distribution from a Roth 401(k), Roth 403(b) or Roth 457(b), it will be tax free.

Timing your RMDs

Most account owners must take their initial distribution by April 1 of the year *after* they turn 70½, though they can take it during the year in which they actually turn 70½. Waiting until the following year to take your initial distribution may have negative ramifications, however: Because you'll be taking two taxable distributions within the same year, you may end up in a higher tax bracket.

What's more, the amount of the second distribution must be calculated using the account balance from Dec. 31 of the previous year — not based on the balance remaining after the first RMD is taken. As a result, the RMD will be larger, increasing the chance you'll be pushed into a higher bracket.

After the initial RMD, you'll need to take subsequent ones by the end of each calendar year. The IRS allows distributions to be taken in installments during a calendar year, so long as the total by the end of the year equals the RMD.

You're free to make withdrawals in excess of your RMD. This will reduce the balance used to calculate your RMD in future years. However, the excess over the RMD you withdraw one year doesn't count toward your RMD in another year.

For example, let's say last year you had a balance of $100,000 in an IRA, and you withdrew $5,000 rather than your RMD of $3,000. This year, your RMD is calculated on $95,000 ($100,000 less the $5,000 you withdrew), and let's say this results in an RMD of $2,500.

That's lower than what your RMD would have been based on the $97,000 balance you would have had in the account if you hadn't withdrawn the extra $2,000 last year. But you can't apply that extra $2,000 to your 2011 RMD to withdraw only $500. You still must withdraw the full $2,500 RMD this year.

Keep the IRS happy

If you've been enjoying your retirement without having to tap your retirement fund, that is fine by the IRS — until you turn age 70½. This is when you must begin taking RMDs, and neglecting to follow these regulations can lead to stiff penalties. Your tax advisor can help you determine your RMD and whether you should take distributions in excess of it. ◈

Make charitable gifts from your IRA

Thanks to a provision in last year's Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act, you can fulfill your required minimum distribution from a retirement plan while also making a contribution to a charity. But unless Congress extends it, this option is available only through 2011.

Under the provision, a nontaxable distribution can be made directly by the trustee of an IRA (other than an employer-sponsored IRA) to an organization that's eligible to accept tax-deductible contributions. You must be at least 70½, and the maximum allowed on an annual basis is $100,000. Thus, even if you've made a $100,000 qualified charitable distribution in a prior year, you are still eligible to make one up to that amount for 2011.

You can achieve similar results by withdrawing the money, donating it to charity and deducting your contribution. But a direct distribution can be simpler, and it also avoids income-based phaseouts that apply to charitable deductions.

Multistate taxation efforts ramp up

Be aware of states with which your company may have nexus

Before a business transaction triggers income or sales tax in a particular state, the company involved typically has to have a nexus — that is, a connection or link — with the state. Until recently, nexus generally was presumed to exist only if the business had a physical presence, such as an office or employees, residing in the state.

Now, the traditional view of nexus is changing. As a result, even businesses without a physical presence in a state may be obligated to pay its income or sales taxes.

Extending nexus

One reason for the change in thinking about nexus is the fact that many transactions today occur electronically. As a result, a physical presence in a state no longer is needed for transactions to occur. This helps states make a case for extending nexus.

And as states struggle to balance their budgets, the idea of extending nexus to more transactions is gaining urgency. Going into the 2012 fiscal year, 45 states and the District of Columbia were projecting budget shortfalls totaling $125 billion, according to the Center on Budget and Policy Priorities. As a result, many state budget officers are eyeing the potential for additional revenue through so-called "Amazon taxes," referring to the behemoth Internet retailer.

Criteria to establish nexus

Nexus also can get complicated because states have different criteria for determining just what triggers their income or sales taxes. To add to the confusion, a state may have one set of criteria for income tax and another set for sales tax. Some questions state governments may use to determine nexus include:

- Does the company regularly market in the state?
- Does it maintain a place of business in the state, on either a temporary or permanent basis?
- Does it have employees or independent contractors in the state?
- If so, do they use company equipment, such as computers?
- Does the company keep inventory in the state?
- Have company executives signed a contract in the state?

Several attempts have been made to simplify the confusing array of state income and sales tax rules. For instance, the Business Activity Tax Simplification Act of 2009 would have, among

other changes, prohibited state taxation on an out-of-state entity that lacked a physical presence in a state. The bill was proposed during the 2009-2010 session of Congress, but never became law.

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The Streamlined Sales and Use Tax Agreement is an effort undertaken, so far, by 44 states and the District of Columbia. It was created more than 10 years ago by the National Governors Association and National Conference of State Legislatures, and includes uniform tax definitions and administration and rate simplification, among other features.

These changes streamline both sales tax collection for state governments and the process of filing sales tax returns for businesses. For instance, all states that are party to the agreement define clothing in the same way. However, some may tax clothing, while others may not.

Another effort is the voluntary disclosure program from the Multistate Tax Commission. This allows an entity that may have potential liability in multiple states to negotiate a settlement agreement regarding back liability. This program also operates in a vast majority of states as well as the District of Columbia.

Obtain a nexus study

Because the regulations surrounding nexus are complicated and changing, familiarize yourself with the criteria used to indicate nexus, and work with your tax advisor to analyze your company's connections to different states.

Undertaking what's often referred to as a "nexus study" can reduce the likelihood that your company inadvertently overlooks any tax obligations created by its nexus to a state. That lowers the risk it will have to pay accumulated taxes and penalties down the road. ◈

Managing your management team

A successful family business requires efficient, informed decision makers

Running a successful family business in today's unsettled economic times requires quality products and services, a talented staff and the ability of managers to efficiently make informed decisions. If your management team members aren't working off the same page, you need to turn your attention to making them better decision makers.

A shared understanding

Start by applying a collaborative approach with the goal of creating a shared understanding. Develop and clearly communicate your company goals and priorities to management team members, so they'll work together and make decisions in line with your family business's direction.

If your goal is to target a product or service to a new market, for instance, you don't want to have employees spend all their time and your resources on existing markets. So constantly update managers on what you're aiming for.

Collaboration has other benefits as well. More individuals participating in decision-making can mean more creative and well-thought-out decisions.

A collaborative approach also distributes the decision-making burden, so it doesn't fall on just your shoulders or those of chief officers. Particularly as your family business grows, sharing responsibility for decisions becomes vital to facilitate progress and seize opportunities.

Know the business inside and out

Improving management's decision-making capabilities also means developing knowledge about your company's overall business and environment. The management team must know the company's operational functions, market positioning strengths, weaknesses, opportunities and competitive threats, and market forces and trends, including supply and demand.

Developing a base of insightful knowledge about your operations and market environment is commonly referred to as "business intelligence." Gathering business intelligence provides management with relevant, quality information needed to make decisions. This knowledge will also help managers anticipate and quickly and efficiently react to changes.

Fortunately, many software applications facilitate data collection, storage, analysis and reporting. For example, you can use enterprise management software to develop business intelligence for such operational functions as human resources, financial, supply chain and customer relationship management.

Leverage each manager's strengths

Creating an effective management team also requires managers to learn to tap one another's skills and collaborate on solutions to challenges and decisions that affect your family business's strategic direction.

To unite your managers into a power team, begin by assessing performance. This entails a confidential review of interpersonal and other leadership, technical and business issues that may be affecting your team's effectiveness. To make the process objective, leave the task to an outside consulting firm specializing in executive assessments.

A collaborative approach distributes the decision-making burden, so it doesn't fall on just your shoulders or those of chief officers.

Assessments may be customized based on your family business's needs. They generally consist of some combination of in-depth, face-to-face executive and group interviews and online or written evaluations. Feedback is provided via written reports and debriefing sessions on both an individual executive and overall team basis. The purpose of the feedback is to provide insights into individual and group strengths and weaknesses, team dynamics, barriers to success, recommendations for improvement, and untapped opportunities.

Add adventure to the mix

One way to make use of executive team assessment feedback is to send your managers on a retreat. Doing so will help managers bond and learn to leverage one another's skills and knowledge for the benefit of the organization. Executive retreats typically follow a more intense format than staff team building events and may be structured to your business's needs.

Retreat options are limited only by a team's creativity, physical abilities and budget. In any case, the end goal is to break down functional silos and communication barriers and establish a strong unity.

To fully realize the potential value of the above activities, you must follow up. That means combining the feedback from the group assessment with the experiences from the retreat into an action plan for furthering the development of teamwork back at the office.

Objectivity can be helpful

Although your primary focus is making quick and efficient decisions, at times you may need to slow your management team down and run a little interference. When family members work together in a business, emotions can sometimes create bias and impair their professional judgment. At such times, they may not act in the family business's best interests, particularly when it comes to nonfamily employees.

If you're facing difficult decisions with complicated ramifications, there's nothing wrong with seeking outside help to gain a more impartial, independent perspective. Try consulting a family business advisor or establishing an advisory board.

Working in concert

Your management team's ability to make quick, informed decisions can mean the difference between the success and failure of your family business. With so much at risk, it's worth the time and money to ensure your top executives are working in harmony. ◈

Does your home office qualify for a deduction?

Whether because their employer is trying to save money on office space or they're self-employed, many people are working from home today. A tax-related benefit of working from home is claiming the home-office deduction. But there's a catch — you must:

- Maintain a specific area in your home that you use regularly and exclusively in connection with your business or trade, and
- Use the area as your principal place of business or, if you also conduct business elsewhere, use the area to regularly conduct business, such as meeting clients and handling management and administrative functions.

If you're an employee, there's an additional requirement: Your home office use must be for your employer's convenience, not simply your own.

Assuming your home office qualifies, you can deduct *direct* expenses, including business-only phone and fax lines, utilities (if you have a separate hookup), office supplies, painting and repairs, and depreciation on office furniture.

You may also claim a percentage of *indirect* home-office expenses, including mortgage interest, property taxes, association fees, home insurance premiums, utilities (if you don't have a separate hookup), costs associated with a security system, and depreciation (over a 39-year period). The percentage allowed is based on how much of your home is dedicated to your home office. Your tax advisor can help you determine the correct percentage.

If you're an employee, you must claim these expenses as a miscellaneous itemized deduction, which is subject to a 2% of adjusted gross income (AGI) floor. This means you'll save taxes only if your home office expenses plus your other miscellaneous itemized deductions exceed the floor.

If you're self-employed, the AGI floor doesn't apply but the home-office deduction can't exceed your self-employment income for the year. If you have more expenses than self-employment income for a given year, you can apply them against your self-employment income in future years.

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Raising the FBAR…

Failure to comply by 6/30/11 may result in civil or even criminal penalties!

TAX FACT: If you have a financial interest in, or authority over a financial account in a foreign country, you are probably facing an additional tax filing requirement with the IRS.

WHAT IS THE FBAR FILING? FBAR is your Foreign Bank Account Reporting Form TD 90.22-1. This is a filing separate from your US Income Tax Return and is due **no later than June 30, 2011**. This can be an extremely complex filing, especially when trusts, pensions, or foreign entities are involved.

The right **ideas**.

The right **results**.

Achieved with the right **firm**.

WHAT YOU NEED TO KNOW: Account holders that fail to comply may be subject to **civil and/or criminal penalties.** These penalties could be up to 50% of the account balance or imprisonment.

Visit our web site to learn more about filing requirements or contact Zinner & Co. for more information.

Your Success is our Business.

ZINNER & CO. LLP

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