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Are You Putting Too Much Money Back Into Your Business?

When you started your company, no doubt investment capital was at a premium. Many entrepreneurs borrow from family and friends, tap home equity, and run up credit card balances to the limit. Though risky, that's just the cost of following a dream. But now, with your business humming along, you may face a different risk. Failing to take money out of the company could imperil your long-term personal financial health.

One problem with paying yourself too little and not funding retirement savings is familiar to anyone who remembers the corporate meltdowns early this decade. When erstwhile Wall Street darlings suddenly crashed and burned, employees were left holding virtually worthless company shares. A similar fate could await owners of small businesses who keep most of their net worth tied up in company stock. If you've poured all of the profits back into the business, what will you be left with if it ultimately fails?

And even if it keeps growing, at some point you need to ask yourself exactly what you hope to accomplish. Are you planning to take the business public someday, generating a big, long-deferred payday for you and the company's other investors? Do you hope to hand off the business to another member of your family? Or are you simply plowing money back into the business for growth for its own sake?

In some scenarios, it may make sense to reinvest as much capital as you can. But the road to an initial public offering is long and treacherous, and very few small businesses ever get there. And what if the heir you're counting on to take the reins ends up having other plans? Though there are plenty of other ways to exit a business, including a sale to a competitor or to your own workers through an employee stock ownership plan, those options, too, put off your ultimate payday and assume the company will continue to thrive.

Instead, you could approach your role with the business as if you were leading a major corporation. Though corporate executives may defer some compensation, they also make sure to receive generous salary packages and fully funded retirement plans. They realize that while they may be on top now, that could change overnight. They also want to be able to live well, enjoying the perks of success while still young and healthy.

How much should you take out of your business? And what are your options? You might start with your own compensation. "Pay yourself first" is

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Yes, We Are Still Accepting New Clients

Now that our offering has expanded beyond investment management to wealth management, one of the most common questions people ask us is whether we are accepting new clients. The answer is yes!

In fact, our minimum fee for new clients is now aligned with the comprehensive services we now offer. When we create a wealth management plan, it encompasses investment consulting, advanced planning, and relationship management.The **advanced planning** portion addresses areas such as wealth enhancement, wealth transfer, wealth protection, and charitable giving. With **relationship management,** we act as a general manager, coordinating our clients' relationships with other professionals such as CPAs, attorneys, and insurance professionals.

Our ideal client is a successful executive or small business owner in the Front Range who is planning for retirement (or already in retirement) and is concerned about preserving and protecting his or her wealth in addition to maintaining a long-lasting, sustainable retirement. The first step in our process is to sit down with a prospective client in a discovery meeting to explore whether the possibility of working together would be mutually beneficial.

If you know of anyone who fits this profile, please have them give us a call. Thanks for your support.

Sincerely,

Robert J. Pyle

Avoid Being Accused Of Insider Trading

Investor confidence in corporate management is at a low ebb. These days, questions normally reserved for corrupt politicians—what did you know and when did you know it?—are being directed at CEOs and other company insiders who have bailed out of multimillion dollar stock positions just before the share price fell off a cliff.

Still, executive compensation often includes large blocks of stock, and, as an insider, you may need to sell shares to finance big purchases, fund a child's education, or simply pay bills. Yet you may also possess nonpublic information about events that could affect your company's share price, and unloading stock under those circumstances could subject you to insider trading charges by the Securities and Exchange Commission, to say nothing of suits by angry shareholders.

The solution? As part of its Regulation FD (for "fair disclosure"), which took effect October 23, 2000, the SEC established rule 10b5-1, which creates an affirmative defense for executives of public companies who buy or sell stock according to a pre-set plan. The idea is that inside information can't come into play if you commit yourself in advance to certain transactions.

Rule 10b5-1 delineates three kinds of permissible contracts: a document specifying trades that will occur at certain prices on particular dates; a plan spelling out a formula that will be followed to determine trades; or a document granting an

independent third party without inside information the discretion to make trades on your behalf.

A simple plan might say that 5,000 shares would be sold May 31 at $15 a share or higher. Or you could base your plan on a formula, stipulating that 10 days after the start of each quarter you would sell enough shares to raise $25,000. Another plan might call for your advisor to dispose of 1,000 shares each quarter, but only if the share price is at least 80% of the stock's 52-week high.

A plan might also mandate selling shares at a specified time to raise funds. According to the SEC, the "formula could provide, for example, that the employee will exercise options and sell the shares one month before each date on which her son's college tuition is due, and link the amount of the trade to the cost of the tuition." Or you could specify that a grant of employee stock options be exercised when the share price rises a certain amount above your exercise price.

As helpful as this rule may be, it does mean giving up some control of what happens to your stock, and you could find yourself selling shares into a slumping market, or raising money and incurring taxable capital gains at a time when you don't need the cash after all.

Lawyers recommend that SEC filings disclose pre-set trading plans.. SEC officials remain concerned about improprieties in this area and have vowed to take a long, hard look at such plans. ●

Passing More Than Money To Your Heirs

In the 2006 film *The Ultimate Gift*, spoiled young Jason Stevens expects a large inheritance from his eccentric grandfather. But when the man passes away, his will stipulates that Jason will get the money only after he accomplishes 12 unusual, demanding tasks. Each is designed to change the way the young man views wealth, human relationships, and the meaning of life.

You're not likely to demand that kind of quest from your heirs. These days, though, it's not unusual to include provisions in a will or estate plan that go beyond financial wealth and relate to personal or social values. It may be possible to encourage your children or grandchildren to continue a family tradition of philanthropy, for example, or to understand the important role your ethnic heritage has played in your life.

But it's tough to pass along your values if your heirs don't know who you really are. Whereas we once routinely gained wisdom and perspective from our elders, that opportunity often gets lost in the shuffle of fast-paced contemporary life. Yet young people still long to comprehend what their families stand for and to feel a sense of belonging and purpose.

Family storytelling is the most natural and direct means of imparting essential elements of your identity. Around the family table, young people can share in the evolution of your attitudes, traditions, and values. When were you happiest? How did you first experience kindness, self-sacrifice, ambition, and generosity? What were the things that mattered to you as a young person, and how have your views changed? What were the turning points in your life, and what do you wish you'd done differently? Though you may worry young people will be bored by your stories, chances are they'll be engaged, especially when the conversation involves them, too. Listening carefully as they relate their own experiences can help you gauge

Planning Ahead A Couple Of Generations

U.S. estate tax laws have been in flux for most of a decade, and the biggest changes are yet to come. Unless Congress dictates otherwise, the individual estate tax exemption is due to jump from $2 million in 2008 to $3.5 million in 2009. The following year, there's an unlimited exemption (in other words, no estate tax at all), and in 2011, the exemption drops to $1 million. Yet as crazy as all of this may seem, a standard estate-planning tool—the "dynasty" trust—can help you avoid problems.

A dynasty trust, a type of generation-skipping trust, is an irrevocable trust that could benefit several generations of your family. Set up correctly, it can help you sidestep gift and estate taxes while also shielding trust assets from creditors. And the sooner you establish the trust, the longer its assets will have time to grow.

With a typical dynasty trust, you'll designate your children and grandchildren as discretionary beneficiaries. Then, when your children die, the trust remains in effect for their children, with payments continuing for generations. Because beneficiaries don't own the assets—instead, they receive income from the trust—there are no estate taxes when a beneficiary dies. That lets the principal keep growing, and assets may be shielded from divorcing spouses, court judgments, and other creditors.

When considering a dynasty trust, there are several tax rules and exemption amounts to keep in mind. The exemptions from estate tax also apply to something known as the generation-skipping transfer (GST) tax, which applies to gifts to generations beyond your children. Moreover, everyone is entitled to a $1 million lifetime exemption from gift tax liability, plus you can make yearly tax-free gifts of up to $12,000 to as many beneficiaries as you like, as long as a "Crummey" provision is diligently applied and executed.

In establishing a dynasty trust, it makes sense to embark on a simple wealth transfer program, making annual $12,000 gifts to all of your children and grandchildren. Your spouse can do the same. If you designate, say, eight yearly recipients, together you'll be able to move $192,000 out of your estate each year. In 10 years, that's almost $2 million.

Your next step could be to fund a dynasty trust with $1 million (or $2 million for a couple), using up your lifetime gift tax exemption. There's one catch, though. Gifts in excess of the $12,000 per year reduce your estate tax exemption dollar for dollar. So if you start a trust with a $1 million gift and then die in 2009, for example, your estate will be able to exclude only $2.5 million from estate taxes, not the $3.5 million otherwise allowed.

And if you'd like to begin the trust with more than $1 million, perhaps using up the higher GST exemption of $2 million in 2008 (or $3.5 million in 2009), a lifetime qualified terminable interest property (QTIP) trust could help. A QTIP trust allows the surviving spouse to use the trust property with taxes deferred until his or her death, after which the trust property goes to the final trust beneficiaries, who were named by the first spouse to die.

The federal government imposed the GST tax in 1986 to prevent people from using trusts to circumvent estate taxes of the next generation of heirs. Now, you can take advantage of the recent increases in the GST tax exemption by making lifetime gifts to a QTIP trust of up to the GST exemption amount.

Then, through your spouse's will, stipulate that upon the spouse's death, any estate taxes on this money will be paid with funds from his or her estate, outside the QTIP. That would allow the trust assets to pass to future generations without being reduced by estate taxes.

The longer a trust continues in existence, the greater its potential appreciation. To extend the life of a dynasty trust as long as possible, set it up in a state that allows such trusts to continue for hundreds of years or in perpetuity—which is the point of a dynasty trust. Most states have laws forcing trusts to terminate 21 years after the death of the last beneficiary living at the time the trust was created, though more and more states are extending that time limit. If you don't reside in a state that has repealed or extended the maximum term for trusts, consider establishing your trust in another state with more favorable laws. That's permitted as long as the trust has some connection to the state. One simple way to meet that requirement is to choose a trustee there, which could be a corporate trustee. But, be aware there is not yet any case law sustaining the effectiveness of a dynasty trust established in a state other than the state of the beneficiaries' residence as it relates to asset protection.

We can work with your attorney to help you decide whether a GST, dynasty, or QTIP trust makes sense as part of your long-term financial and estate plan. ●

their values and ambitions.

Of course, just helping your heirs get to know you doesn't ensure they'll carry on your passions. Yet there are ways to expose your children and grandchildren to organizations that matter to you, and to get them involved in your cherished causes. You can take them along when you attend meetings and events, and make sure they connect with key people. Your estate plan can help too:

- Set aside assets to help heirs visit your family's country of origin or places significant to your family's heritage
- Provide funding for family members' business or educational development
- Launch a 501(c)(3) nonprofit organization (or establish a community foundation "support organization") and name family members to the board of directors
- Establish a charitable remainder or lead trust that links philanthropic and financial interests. This can become a donor advised fund upon your death.

Create a donor-advised fund and let younger family members recommend grant recipients

Discussions with your family can form the foundation of a values-based blueprint. We can help you start these conversations and work with you and your attorneys to create an estate plan that incorporates your goals. ●

Limits Of Family Limited Partnerships

In recent years family limited partnerships (FLPs) have become an increasingly popular way to give assets to children. You can discount the value of assets you transfer to an FLP by 20%, 30% or even 50%. The less a gift is worth in the eyes of the IRS, the more you can pass along with little or no tax liability. Thus, you can transfer an interest in a business, real estate, securities, or other holdings to your children and pay lower gift and estate taxes.

One of the key attractions to FLPs has been the ability to give away discounted interests in your assets while continuing to manage them. Now, however, a U.S. Tax Court decision has called into question the ability of those who establish FLPs to retain management control

Typically, parents establish an FLP to hold a particular asset. They serve as general partners and manage the FLP, while the children are limited partners. Because the children couldn't easily sell their interests in this private vehicle managed by their parents, the IRS considers interests in an FLP to be worth less than the actual market value of assets it holds. So, for example, a gift of a 99% limited partnership interest in an FLP owning property worth $1.5 million might be valued at just $1 million for tax purposes.

For wealthy families with many children and grandchildren, an FLP can be a good way to move assets out of parents' estates. Because anyone can make annual tax-free gifts of up to $12,000 to an unlimited number of recipients, parents can slowly transfer assets to their family's younger generations without paying gift tax. An FLP can also be an effective way to transfer real estate incrementally without having to file a new deed every year.

The Tax Court decision in May 2003 invalidated an FLP established by Albert Strangi. The problem, the court ruled, was that Strangi, through his attorney, still had use of the assets he was transferring, and as general partner retained the right to determine who could enjoy them. The court threw the full, undiscounted value of property contributed to the FLP back into Strangi's estate for tax purposes.

Subsequently, the decision against Strangi was affirmed by the Fifth Circuit Court.

Despite this turn of events, FLPs are still very much alive, although some concessions may have to be made. For instance, parents transferring assets to children may have to give up management control of the FLP, say estate tax attorneys. One way to do that could be to name your spouse as general partner, says Gideon Rothschild, chairman of the American Bar Association International Estate Planning Committee. But you, and not your spouse, would have to transfer the assets, Rothschild says. Another approach would be to name a trust with an independent trustee as GP. Rothschild says that another recent court case confirmed the validity of FLPs when the transferring party didn't retain an interest in the assets. He maintains the Strangi case doesn't negate the benefits of FLPs; it just requires more careful crafting and a rethinking of the management structure. ●

Too Much Money Back In

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timeworn advice, but it's also essential, and in developing the annual budget for your company, begin by penciling in competitive compensation for yourself. Once you acknowledge that as a necessary cost of doing business, it will become less of an issue as you chart plans for future growth. And the money you take home will be a tangible reminder of what you've been working so hard to achieve.

For retirement savings, there are many possibilities. If you have done little so far or simply want to pull out maximum cash from your business, a defined-benefit plan could help. Here, you work backward from a specified future benefit to determine how much your annual contribution must be. In most cases, this requires actuarial calculations taking into account years to retirement, life expectancy, and other factors, and you'll need to fund future benefits for a number of your employees as well. Businesses with only a few workers can consider off-the-shelf defined-benefit plans, while plans built around annuities or life insurance might enable you to set aside several hundred thousand dollars a year. And all of the company's contributions are tax-deductible as a business expense.

A wide range of defined-contributions plans, from garden-variety 401(k)s to SIMPLE and SEP IRAs and profit-sharing plans, could also help you pull out money from your business while reducing taxes and providing retirement income. One major advantage of such plans is that, unlike defined-benefit plans for which annual outlays are mandatory, you may be able to contribute less in years when business is slow. And while annual contribution limits are lower for defined-contribution plans, your business could use both kinds of plan to maximize tax-advantaged savings. Moreover, 401(k)s and most other defined-contribution plans offer relatively broad investment options that can help diversify your retirement savings.

We can work with you to sort through the many options for funding your current and future compensation and will gladly answer whatever questions you may have on these topics. ●

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