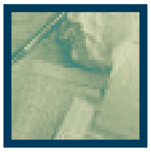
Summer 2003



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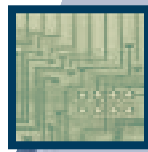

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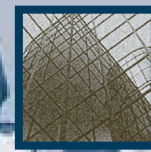


GROWTH

BUSINESS *i*NSIGHTS

*i*NSIDE

9 Ways To Boost Cash Flow *Now*

PROFIT IMPROVEMENT

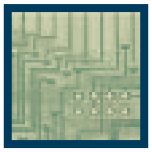
You've heard it said, "Cash is king." That statement rings truer than ever when credit is tight. Even profitable businesses can and do end up in bankruptcy because they run out of cash to meet their needs. So, how do you ensure your cash keeps flowing? While not all are appropriate for every business, these tips will help:

1. Forecast your cash inflows and outflows. Most are very predictable. By modeling projected cash flow, potential problems can be identified in advance and dealt with. For instance, a new line of credit may need to be established to build up inventories before the holiday season or a major expenditure may need to be delayed.
2. Don't just negotiate price with suppliers, try to negotiate liberal payment terms. You may be able to get the supplier to basically finance your inventory or even sell to you on consignment.
3. Conversely, with customers, make prompt payment part of the negotiation along with price. By explicitly discussing payment terms up front, you can establish an expectation of prompt payment in the customer's mind.
4. Speed up your billing cycle. It may even be feasible to bill in advance of delivery. Billing more promptly will have a direct impact on accounts receivable days outstanding.
5. Speed up collections by following up promptly and assertively on past-due balances. If feasible, encourage the use of credit cards instead of keeping open accounts. Resolve customer billing disputes as quickly as possible to minimize slow payments, and charge interest on past-due balances.
6. Eliminate cash advances. Issue company purchasing or credit cards to employees who travel or make reimbursable purchases. Having clear policies on allowable expenditures and requiring detailed receipts will minimize inappropriate spending and fraud.
7. Use long-term financing to pay for large capital items or lease them. While there is certainly a cost to this strategy, it spreads the cash outlay over a long period of time.
8. Keep inventories at the lowest possible level. It not only conserves cash, it can boost profits by cutting finance charges, lowering the risk of write downs due to obsolescence, and reducing storage costs.
9. Perform credit checks on new customers and even periodically on established customers. Large, new customers can be a particular risk because of the extraordinary expenditures that often need be made before the goods or services are delivered and payment is received. With these customers, go beyond a simple credit check. Dun & Bradstreet reports, which are references from other companies that do business with them, can be very useful.

As your CPA we can set up a process to forecast your cash needs and help you implement these and other cash-boosting, profitability-enhancing strategies. We can also examine tax strategies that will help boost your business' cash flow. Call us! ■

iNSIDE

VPNs – Meeting The Security Needs Of Business Networks



COMPUTERS

Connecting remote workers, home and branch offices, and business partners economically yet securely has always been a challenge. Dedicated leased lines are expensive, direct telephone dial-up is too slow, and connecting through the Internet can potentially compromise company systems and sensitive data.

Enter the virtual private network (VPN). It's a solution that combines the economy and ubiquity of the Internet with the security of a private network. And the good news is that, although they've been around for a few years, VPNs are now cheaper and easier to use than ever.

How A VPN Works

A VPN uses the Internet like a secure private network by creating what is known as a "tunnel" through cyberspace, encrypting data at the sending end and decrypting it on the receiving end.

In a traditional VPN, software sits on a computer at each end of the Internet connection to perform the encrypting and decrypting functions. This works well for office-to-office connections. However, for connecting with individual remote workers, this solution is more challenging because the VPN software must be installed on the individual workers' PCs. This often means it's necessary to send a support person out to load the needed software on home computers.

To address this issue, vendors have recently introduced a VPN that utilizes Secure Sockets Layer encryption (SSL). This technology, which is supported by all Web browsers, is the same technology used on Web sites to provide privacy for credit card transactions.

The disadvantage of this approach is that it only provides access to Web-compatible applications. So, if an order entry system doesn't have a Web front end, it cannot be accessed through this type of VPN. Fortunately, more and more applications software vendors are adding Web access to their products.

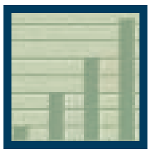
Implementing A VPN

Besides determining whether a traditional or an SSL VPN is the best approach, there are a number of other factors to consider before implementing a VPN. A VPN can either be purchased as simply software to be loaded onto a business' servers and PCs, or bundled into special purpose hardware appliances that plug into a company's network. The appliance option typically is simpler to implement and support, but may be less flexible. Whichever option is chosen, purchasing products that support industry standards (IPSec, MPLS, and SSL) is critical to making a VPN connection to another party.

An important consideration in deciding whether a VPN is appropriate is the need for consistent bandwidth. While a VPN overcomes the Internet's security weaknesses, it does nothing to address the variation in data transmission speed that can occur when Internet traffic gets extremely heavy. For this reason, a VPN may not be the best solution for voice or video, or when very quick, consistent response time is needed.

Many businesses are implementing VPNs to address their remote access needs. For those in financial services and health care, privacy regulations make it the only practical solution in many situations. For others, it's just the prudent thing to do. New appliances on the market are priced as low as a few hundred dollars and are quite easy to plug right into a local area network. ■

Capitalizing On An Important Strategic Asset – A Board Of Directors



CHARTING YOUR FUTURE

An independent board of directors or advisors can be an important strategic asset. It can help you make critical decisions by bringing together a mix of experience, skills, and objective observation. It can open doors to new ideas, new markets, new partners, and new capital. If you don't have a board, consider forming one. If you do, make sure you're getting as much benefit as possible from that group of people.

Types Of Boards

Almost every corporation has a statutory board of directors, but for many smaller companies it may consist of just the business owners and an attorney. Larger businesses or those with outside investors often have a larger board with independent members. The *board of directors* is legally responsible for governance of the corporation. By contrast, a *board of advisors* is a group formed by the business owner or owners to provide guidance and advice, but without any legal authority.

For many small business CEOs, an advisory board makes more sense than expanding the statutory board. The owner keeps full control and the need for directors' liability insurance, which can be expensive, is minimized.

Purpose, Composition, And Authority

Whether forming an advisory board or a formal board of directors, there needs to be a clear understanding of the board's purpose. Is it to give general business guidance, give the company more credence in the eyes of customers, focus on the business' financial structure, or fulfill another objective?

In the wake of recent financial reporting scandals, does the company need to beef up its audit committee? Where does the owner need help most? The answers should drive the criteria for board membership.

In structuring the board, most experts recommend an odd number (no more than seven) of individuals who are not employees, friends, or relatives. To find appropriate independent board members, look to customers and suppliers, local universities, and referrals from professional advisors such as your CPA, attorney, and banker. The local SCORE (Service Corps of Retired Executives) office is a good source for recruiting retired executives for board duty.

A source of frustration for business owners and board members alike can be a lack of clarity around the board's authority. Even if it's constituted as a formal board of directors, in a private company with a majority owner, it may really act as an advisory board on many issues. Whether in an advisory or decision-making role, the board needs to have the confidence to reach decisions and to fulfill its responsibilities.

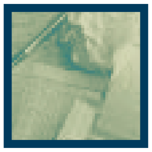
Commitment And Participation

To maximize participation of board members in deliberations, let them know how much time they will have to dedicate when recruiting board members. Then, schedule meetings well in advance and at convenient times. Send out agendas and background materials ahead of time so that the members can be better prepared for meetings.

During meetings, clearly state the objectives and make sure everyone feels their input is welcome. Many experts advise paying board members, even if it's only a modest sum, to strengthen their commitment. It can also be a good idea to have board members sign confidentiality agreements to make the owner feel more comfortable sharing information.

An effective board of directors or advisors is an important asset to the leadership of any business. If you want to form a new board or restructure your current one, look to us to help find the new members to meet your needs. ■

Benchmarking Compensation To Keep Your Business On Track



HUMAN RESOURCES

Competitive pay scales are essential to an organization's health. Pay too much and your expenses will be out of line. Pay too little and qualified employees will be difficult to recruit and hold on to. Human resource professionals utilize salary surveys to keep their pay scales on track. It's important to thoroughly understand these surveys so you can compare "apples to apples."

Sources Of Data

There are a number of places to look for comparative salary information. National and regional surveys are regularly conducted by large HR consulting firms, such as Mercer and Haye. Online, Salary.com offers extensive salary survey data. Professional and industry groups also conduct surveys that they typically sell to their members as well as the general public. While some of these surveys will cost you hundreds of dollars, free salary information is available from Robert Half ***(www.roberthalf.com)*** and ***Monster.com.***

At the local level, contact your chamber of commerce for salary surveys. Groups of local businesses may also commission a survey and all contribute salary data to an independent third party that anonymously compiles the results.

What To Watch For

Raw survey data should not drive pay scales. First, a business needs to decide where it wants to be in the market with respect to salary. Does it want to be a market leader, in the middle of the pack, or below the median? This is a complex question. Some companies believe that premium pay attracts the best employees. Other businesses have managed to attract and retain their workforces with below-average pay by emphasizing other elements of the work experience. A business also needs to look beyond just salary to the value of the total compensation package including bonuses, time off, retirement plans, and other benefits.

Survey data also need to be carefully interpreted. National or regional data may not be applicable to a local market. It can also be tricky to identify comparable positions. Systems analyst or accountant positions, for example, may have a very different scope of duties, education, and work experience from one company to the next. In some surveys the time lag between when the data were collected and the date the survey is published can be considerable; and in other cases, the sample size for a particular job title or locality may be relatively small. It pays to read the fine print and question the author.

Even in today's environment, when the employment market has loosened in many fields, it's important to set salaries at levels that help keep the employees you want to retain and attract the new workers you need – all the while keeping operating costs in check. Salary surveys can be an excellent starting point. We can help you analyze your current salary schedule. ■

Keeping Employees Satisfied

With most annual raises lower than they were just a few years ago, current employees may become dissatisfied with their pay, even though it's still competitive in the market. At times like this, it's important to emphasize other factors that keep employees loyal and energized.

According to a recent Society for Human Resource Management survey, employees ranked these work attributes at the top of the list: the desire to be listened to at work and the desire to receive personal recognition. Other highly valued attributes were the freedom to laugh at work, economic security, and the ability to control one's own decisions.

What To Do When The IRS Comes a'Knockin At Your Door

TAX PLANNING

This may be the year that you hear from the IRS. After several years of declining audit rates, the IRS has vowed to increase examinations and has narrowed their focus to what they believe will be more productive audits.

Besides what the IRS includes in their broad definition of "abusive schemes and shelters," they will target what they term "high-risk, high-income taxpayers," high-income non-filers, and unreported income.

Don't be surprised if you fall into one of these categories. The IRS definition of "high-income" may be what many of us think of as middle-class. The IRS has also recently intensified their analysis of K-1 matching. This could result in questions regarding your reporting of partnership or S corporation income.

The Service has also implemented new National Research Program (NRP) audits. More intrusive than regular examinations, these audits gather data to be used in the selection of future returns for audit. They are designed to address major issues rather than dwell on meaningless details, which was the case under the now defunct Taxpayer Compliance Measurement Program.

Information obtained from these audits will help the IRS make decisions about resources and strategy, education efforts, and (perhaps most importantly) determine which types of returns should be selected for examination.

What Are Your Odds?

Audits of the 50,000 sample NRP returns will continue throughout 2003. The IRS anticipates that for 8,000 returns, there will be no contact from the IRS. Correspondence audits will be conducted for 9,000 taxpayers; 30,000 will undergo limited-scope examinations; and 2,000 will undergo line-by-line scrutiny.

The IRS isn't saying how many returns will be subjected to regular audits – only that the number will increase. So your chances of being audited are greater… particularly if you are in one of the targeted groups.

Notices And Correspondence

Sometimes the IRS chooses to conduct examinations by correspondence. Or, you may receive a notice that purports to correct an error on your return. Although these situations are generally not as stressful, engaging a tax professional who can present information in a manner that meets the IRS requirements can save you a lot of time and effort. Government oversight studies indicate a significant number of "automatic" adjustment notices are wrong, and that many taxpayers simply pay the notices, assuming that they are correct.

Collection Matters

We can also help with IRS collection matters. We can determine if any penalty or interest waivers apply, assist in presenting financial information to the IRS, and help in negotiating payment terms. In some situations, an "offer in compromise" is appropriate. This procedure offers the IRS a reduced amount in order to settle the matter.

In all collection matters, a determination should be made that any and all tax law arguments have been exhausted. Sometimes there is a remedy under tax law, which reduces or eliminates the amount due.

Appeals

Whether you have an examination or a collection matter, you do have the right to appeal. But you must follow specific procedures. If you wait too long in the process, you may miss your chance to have reconsideration at an appellate level.

Get Us Involved

If the IRS calls, writes, or worse – just shows up at your door, call us immediately. We can help make the IRS encounter less painful. We can handle most of the interaction, determine what information is appropriate to provide, and determine how to proceed most efficiently and effectively. ■

Keep 'Em Happy… Develop Creative Compensation Strategies

Business owners must look at compensation three ways: their own compensation, employee compensation, and the business' bottom line. While these may seem like competing concerns, creative compensation planning can benefit all parties.

Compensating The Owner

If you own a closely held or family owned business, you may feel that you are always last in line when it comes to compensation. Here are some ideas for increasing your take from the business:

Create incentive compensation plans. A written compensation formula that rewards you based on profits, or certain measuring events, can go a long way toward making sure you're entitled to more in the good years (and help reduce IRS reclassification as dividends).

Make sure your compensation is "reasonable." The IRS is skeptical of large salaries paid to business owners. We can help you lay the groundwork for reasonable and supportable compensation.

Get paid for everything you bring to the table. Do you have know-how, a patent, formula, or other intangible that the business is using? If so, talk to us about whether some additional form of payment might be appropriate.

Determine whether personal expenses are company expenses. In some cases, the IRS may approve the company picking up the tab for expenses that have some personal benefit. For instance, business succession planning for a family owned business is intertwined with the owner's estate planning. These determinations can be tricky, so talk to us first.

Make the most of retirement plans. Take advantage of all company-sponsored retirement plans and contribute the maximum possible. A combination of plans might increase your allowable contribution.

Employ your spouse or children. This simple strategy allows you to move some company profit into your family's hands (possibly at lower tax brackets). Plus, they can take advantage of fringe benefits, and sole proprietorships may save on payroll taxes.

The form of your business (corporation, S corporation, partnership, LLC, or sole proprietorship) can affect compensation and fringe benefits for owners. So check with us before implementing any of these ideas.

Compensating Employees

A well-thought-out compensation package can appropriately reward employees and makes good business sense. Don't forget… business owners are entitled to these too (depending on your business structure).

Fringe benefits may be better than cash. Many fringe benefits are not taxable to the employee, but are deductible by the company. Compensate with flexible spending plan benefits and fringe benefits, which aren't subject to payroll taxes. Make sure you consider all of the different benefits, such as: insurance, flexible spending accounts, the new health reimbursement arrangements, certain education costs, and possibly some financial and tax planning costs.

Employees like choices. Planning can help you structure compensation favorably and as individually as possible.

Let employees share in the profits. This strategy can be used effectively through incentive compensation, a phantom stock plan, and non-qualified deferred compensation. Also consider the power of incentive compensation based on the company's profits.

Have effective expense reimbursement plans. Re-evaluate the company's business expense policies to ensure that you are getting as much reimbursement as possible and that the plan conforms to IRS requirements.

Creative and effective compensation planning can be a win/win situation. We can help by analyzing how these strategies could work in your business. ■

Practical Uses For Practical Trusts

Here's the shocking truth… unlike what you've always thought, trusts are not just for the wealthy. Many average taxpayers will find practical uses for trusts for their investments, retirement, children's education, and their estates. This article focuses on types of trusts that may be just right for you.

Estate Planning Trusts For "Everyman"

Revocable trusts avoid probate of your assets at death, and married couples can use revocable trusts to maximize their use of lifetime exemption amounts from federal estate tax (currently $1 million). With that said, here are a few uses of trusts to consider:

- Revocable trust to avoid probate. Assets transferred to the trust are not subject to probate upon your death. This saves time and money, and preserves some privacy.
- Revocable trust to maximize use of the unified credit exemption amount (becomes irrevocable at death). Assets can be left for the benefit of the surviving spouse, while still utilizing the first spouse's unified credit exemption amount.
- Life insurance trust. Policies held by a properly drafted trust are not included in the insured's taxable estate. This type of trust is a must for anyone with a sizable insurance policy.
- Qualified residence trust. Putting your home in a trust reduces the potential estate or gift taxes on your personal residence.

It's Not Just About Estate Planning

There are other situations where the use of a trust may help you achieve your objectives. For instance…

Education Trust. If you'd like to help fund your grandkids' college education, you know how frustrating it can be to determine how much each grandchild will need. You could simply give money directly to your children, with instructions for them to use the money for that purpose, but that doesn't guarantee that the money will be available when your grandchildren need it. To ensure this objective, consider establishing a trust and give the trustees (possibly your children or a financial institution) discretion to allocate the funds among your grandchildren as appropriate to provide incentives for them to pursue their higher education. The trust could invest in Section 529 college savings accounts, which would be income-tax-free to the extent they are used to pay education expenses.

Creditor Protection. Many parents have had the unfortunate experience of making large gifts to a married child who subsequently gets divorced and much of those assets go to the former in-law. In other instances, the child may be subject to claims from a lawsuit. A trust can be an excellent vehicle for making gifts to your children in a way that makes the assets available for their use but prevents them from being depleted to satisfy the claims of potential creditors.

Spendthrift Protection. You may have a child or relative who needs your financial support, but cannot effectively manage the assets. A trust can be established that will assure both you and your intended beneficiary that the funds will not be wasted and will be available when they are truly needed. The trust can be structured to distribute assets when the beneficiary reaches a certain age; or to allow the beneficiary to become a co-trustee so that they may participate in, but not have sole responsibility for, management of trust assets.

Medicaid/SSI "Supplemental Needs." If your child has disabilities that may qualify for governmental assistance, the receipt of an inheritance or gift normally will disqualify them from such benefits until the gift is "spent down" until only exempt resources remain. In that situation, it's critical to leave assets in a carefully drafted discretionary trust that permits the trustee to expend needed resources for the child's benefit in a manner which supplements, but does not replace, governmental resource payments.

There are numerous ways for those of more modest means to use a trust in their estate planning and normal life circumstances. Please contact us to discuss whether establishing a trust is right for you. ■

Executive Summary: Jobs and Growth Tax Relief Reconciliation Act of 2003

WASHINGTON ALERT

In a flurry of last-minute activity, Congress passed the Jobs and Growth Tax Relief Reconciliation Act of 2003 (2003 Tax Act) before heading out for the Memorial Day weekend. At less than half the tax cut initially proposed by President Bush, the 2003 Tax Act still contains tax breaks which will affect all taxpaying Americans. Here are the highlights:

For taxpayers in the highest tax brackets, the ***tax rate on capital gains and dividends*** will be lowered to 15% for the years 2003 to 2008. Taxpayers in lower income brackets will pay a 5% tax rate on capital gains and dividends in years 2003 to 2007, and no taxes on such income in 2008. The capital gains relief will be effective as of May 6, 2003; while the dividends provision will be effective as of January 1, 2003. Both types of relief expire at the end of 2008.

Section 179 small business expensing has been increased from $25,000 to $100,000. The phase-out threshold level also increased from $200,000 to $400,000. This is effective for property in service in taxable years beginning in 2003, 2004, and 2005.

"Bonus" depreciation, as established under the 2002 Tax Act (at 30%) has been increased to 50% for property acquired after May 5, 2003 and before January 1, 2005. As with the earlier 30% bonus depreciation, buildings and used property will not apply.

The ***child tax credit*** has been increased to $1,000 for 2003 and 2004. This increase will include advance rebates of up to $400 per eligible child, with checks to be mailed this summer.

The ***10% income tax bracket increase*** has been accelerated so that it will be effective in 2003 and 2004. This gives joint filers an additional $2,000 ($1,000 for singles) taxed at the lowest rate of 10%.

2003 individual tax rate reductions have been accelerated. Reductions scheduled to take place in 2004 and 2006 will now be effective January 1, 2003. Now, the 2003 rates will be 10%, 15%, 25%, 28%, 33%, and 35%, a reduction of 2% to 3% for the top four tax brackets.

Marriage tax relief has also been accelerated; including an increase in the standard deduction and expansion of the 15% income bracket. Both would be twice the amount for singles, effective for years 2003 and 2004.

The ***alternative minimum tax exemption amount*** has been increased to $58,000 for married couples that file joint returns ($40,250 for single filers) for taxable years beginning in 2003 and 2004. This is an increase of $9,000 for couples and $4,500 for individuals.

Many of these provisions apply only for a few years and they all will still sunset after 2010 (as set forth under the 2001 Tax Act).

We may see even more tax legislation this year. Some members of Congress have indicated that there may be two more tax bills in 2003. We'll keep an eye on the legislative happenings.

To receive the most benefit from these tax cuts, talk with us. We will help you with the necessary tax planning. ■