

focus

year end 2009

All hands on deck

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A management issue that's unique to family businesses is keeping *non*-family employees from feeling out of the loop and undervalued on company endeavors — such as key strategic decisions, product development, or client satisfaction and retention — simply because they aren't family members.

Take a quick look at your top managers — are they all family members? If you answered, “yes,” that's fine, but you may want to take steps to keep nonfamily employees informed and motivated. To do so, consider this: a change from a traditional, top-down management style to a collaborative management approach.

Collaborative benefits

A collaborative management environment can help create an “all for one, one for all” attitude among *all* of your employees. This benefit can ultimately translate into higher productivity and profits and can be felt in all areas of your company — from the management level, where the objective may be to cut operational costs or improve employee retention, to the project level, where the goal may be to develop or enhance a product or service.

A collaborative management environment can help create an “all for one, one for all” attitude among all of your employees.

In addition to providing employees a better understanding of their importance in the company, a collaborative environment can improve operational and work efficiencies, provide an appreciation for different ways of



thinking and support for decisions, and spur innovative solutions.

Leadership and motivation

To successfully implement a collaborative management environment, a strong leader who clearly communicates the company vision and rallies team members to fulfill organizational goals is essential. The team leader — a family member or nonfamily member, depending on who possesses the strongest leadership skills — also should provide direction around obstacles and mediate conflicts that may arise among team members.

Your team leader must establish policies and procedures for the team. Otherwise, infighting may erupt when problems arise. Rules to consider include requiring punctuality, preparedness and adherence to deadlines.

To motivate employees to adopt a team-oriented attitude, establish a performance measurement system that emphasizes and rewards teamwork. For instance, evaluate

product development team members on both how they performed their individual responsibilities and how they collaborated with others to achieve the team's goal of a successful product launch. Metrics could include actual total cost to develop and produce and total time to market against targets.

Outside collaborations

In addition to encouraging collaboration internally, there are opportunities waiting beyond the walls of your business. For starters, you can tap the expertise of outside professional advisors, such as your accountant, lawyer or family business coach.

Another great opportunity is to network with other family businesses to discuss common challenges, share insights and work together on solutions. For example, a family-owned manufacturer may consult with family-owned manufacturers of noncompeting products. The business owners can trade experiences, learn from each other's mistakes, and take comfort that they're not alone in the challenges they face.

To find other family businesses to network with, check out industry and business associations, chambers of commerce or your local family business council. Social media sites such as LinkedIn and Facebook also can be useful. Or you could even organize your own networking program, inviting other family businesses to participate in roundtable discussions or deliver presentations on topics unique to family businesses.

Budget permitting, you might offer to sponsor the first networking event and then charge companies who wish to sign up and continue with the program for successive events. The initial investment can pay off with a continuous flow of invaluable insights.

All together now ...

For your family business to operate efficiently and profitably, you need all of your employees working together as a team. Implementing a collaborative management style can help you do just that by keeping nonfamily employees in the loop and giving them a sense of self-worth within the company. ♦

Left a job?

Pay heed to your 401(k) plan

Because of the economic downturn, many people find themselves unemployed. Others have been fortunate enough to still have found new opportunities and have changed jobs. If you're counted among either group, your 401(k) plan, understandably, may not be top of mind. But it's worth your while to pay heed to it.

Flexibility counts

After leaving a job (whether voluntarily or involuntarily), you may wish for greater flexibility in how your retirement money is invested than a 401(k) allows. Why? Typically 401(k) investments are limited by the choices the sponsoring



Break in case of emergency?

No doubt about it, being unemployed can put any family in a difficult financial position, which can become downright harrowing if you incur a large, unexpected expense during this time. For example, if you or a family member gets injured in a car accident, how will you pay your health insurance deductible, or, worse, what if you don't have health insurance because you can't afford COBRA?

During a time like this, your thoughts may turn to cashing out your 401(k) plan. If, as described in the above example, the situation is a medical emergency (and in a few other limited situations), you may have the option of taking out a plan loan. But cashing out your retirement fund should be avoided if at all possible.

The main reason is because you'll lose the nest egg you've been working so hard to build. But you'll also incur stiff withdrawal penalties and accelerate tax liability if you withdraw funds too early. You'll owe federal income taxes and, depending on your state and locality, perhaps state and local income taxes on the withdrawal. If you're younger than 59½ when you make the withdrawal, you'll likely suffer an additional federal penalty of 10%. Further, some states also impose penalties.

In addition, your former employer generally is required to withhold 20% of your distribution for federal income taxes. Finally, by withdrawing funds early, you'll lose their tax-deferred growth potential.



employer makes available — some plans offer a broadly diversified selection of quality funds while others offer only a limited number of funds that offer mediocre returns.

One option — generally available only when you leave the employer sponsoring your plan — is to roll your 401(k) funds into an IRA. With an IRA, if, for example, you wish to own a specific mutual fund or security in your retirement account, you can. Bear in mind that IRAs may charge you modest administrative fees. But these days more and more employers are passing along 401(k) fees to plan participants, so IRA fees aren't necessarily a significant negative.

Perhaps a more important minus is that, unlike some 401(k)s, IRAs don't allow loans. On the positive side, IRAs generally offer you more opportunities to make penalty-free withdrawals *before* you turn 59½.

Direct vs. indirect rollovers

There are two types of rollovers: direct and indirect. A direct rollover — typically the better option — involves never taking formal possession of the funds. When using a direct rollover, your 401(k)'s administrator transfers your balance to your IRA's custodian, such as a bank or brokerage firm. (The check may instead be mailed to you and then you'll have to pass it on to your IRA custodian. In any case, as long as the check isn't personally made out to you, the transfer of funds is considered a direct rollover.)

An indirect rollover is a bit riskier if you don't strictly follow the rules. This method involves you taking personal possession of your 401(k)'s assets before rolling them over into your IRA. Once you have the funds, you have 60 days to redeposit them into your IRA, via your IRA custodian. If you're tardy, the IRS will consider this a distribution, and you'll owe income taxes and, generally, if you

are under 59½, an additional 10% early withdrawal penalty.

Also, when you opt for an indirect rollover, your former employer is required — except in limited circumstances — to withhold 20% of your 401(k) account value to pay federal income taxes, even though your rollover is considered tax free if you abide by the 60-day rule. Bear in mind that, when you roll the funds over to the IRA within the 60-day timeframe, you'll need to roll the entire 100% or you'll have to include the 20% amount as additional income — and the amount that you don't roll over will, if applicable, be subject to penalties. Fortunately, the amount withheld can be refunded when you file your tax return. But this may be many months later.

After leaving a job, you may wish for greater flexibility in how your retirement money is invested than a 401(k) allows.

For example, suppose Joe, who is 35 and doesn't meet an exception for penalty-free withdrawal, wishes to do an indirect rollover with his \$10,000 401(k) balance. He'll receive a check for \$8,000, based on his \$10,000 balance less 20%, or \$2,000, withholding.

If he rolls over anything less than \$10,000, he'll need to include the difference in income and will be subject to a 10% penalty on that amount. So, if he rolls over the \$8,000 that he actually received, he'll pay tax on the \$2,000 and be subject to a 10% penalty on the \$2,000 amount. In addition, he'll be able to claim the \$2,000 withholding. If, however, Joe does a direct rollover, he'll avoid the additional tax and penalty, and his retirement account balance will still be at \$10,000.

Happy with your 401(k)'s performance?

If you're satisfied with the return your 401(k)'s investments are generating, feel free to keep your retirement plan status quo. So long as you have at least a \$5,000 balance, your former employer can't force you out of its plan.

But don't forget about your account entirely. You must be mindful of any applicable regulations and restrictions, such as revised minimum balance requirements.

Evaluate your options

Whether you've been laid off and your career temporarily disrupted, or you've recently made a move to advance your career, don't forget about your 401(k) plan. You might benefit by taking this opportunity to roll it into an IRA. Or it may make sense to maintain your 401(k). The important thing is to take the time to evaluate your options. ♦

Structure your company around the right business structure

When Kate started her garden center business 10 years ago, she had to make several important, complex decisions. One such decision was which business structure to use — a sole proprietorship, partnership, corporation (C or S corporation) or limited liability company (LLC).

Kate settled on a sole proprietorship because it was the easiest to set up and she didn't have business partners. But in the intervening years, Kate's business has grown, and she's learned more about the interrelated tax, liability and administrative factors of the other business structures. She's now wondering

whether she made the right structure choice. The good news is that Kate can choose a new business structure, but which one? If, like Kate, you're wondering if you should change business structures, the first step is to review the main types.

Sole proprietorships and partnerships

In a sole proprietorship, the business's owner has complete control and ownership and reports all business income or losses on his or her personal income tax return. This relatively simple and least expensive to set up structure, however, has a substantial downside: risk. Sole proprietors put both their business and personal assets at risk because they're personally liable for all debts and lawsuits against their businesses.

With a partnership structure, two or more people (or entities) own the business. For tax purposes, every partner is a co-owner, and for control purposes, a partnership agreement is drawn up to dictate how:

- ◆ Decisions will be made,
- ◆ Profits, losses and liabilities will be shared,
- ◆ Disputes will be resolved,
- ◆ Partners can be bought out, and
- ◆ The partnership will be dissolved, if needed.

Even though a partnership itself doesn't pay federal income taxes, it does have to file an informational return. And as with a sole proprietorship, the individual partners report their share of profits and losses on their personal tax returns.

There are two types of partnerships: general and limited. Under a general partnership, all partners are personally liable for the company's debts; however, partners can make business decisions without consulting the others. Under a limited partnership, only the general partners have unlimited personal liability for the partnership's debts, and they also are the only partners who can make business decisions.

C and S corporations

As a business grows, so do its risks. To protect themselves from personal liability and lawsuits, many owners choose to incorporate.



For tax purposes, a corporation and its owners (shareholders) are considered separate entities. Therefore, the owners are shielded from personal liability; only the business's assets are at risk. In other words, owners' personal assets are safe from creditors if the company falls on hard times, unless the shareholder has personally guaranteed the debts of the company.

There are two types of corporations, and the main difference between them is how the corporation is taxed.

A C corporation generally isn't a popular choice because the company's profit is subject to double taxation. The corporation pays tax on its profit and then the shareholders pay tax on the dividends received from the corporation.

An S corporation generally avoids the double taxation problem. How? As with a partnership, profits and losses flow through to shareholders, who are then each responsible to report the income or loss on their personal tax return and pay tax at their individual tax rate. Distributions are based on ownership percentages. Generally, an S corporation doesn't pay any tax. But S corporations are subject to various limitations, such as the number of shareholders and the types of entities that can be shareholders,

which can make them less attractive for some businesses.

LLCs

An LLC offers business owners the best features of an S corporation without as many limitations. An LLC's profits and losses typically are passed through to its owners — who are called members — without the restrictions imposed on S corporations.

Another LLC advantage is that the company can change its business structure to a corporation in the future without incurring major tax consequences.

On the negative side, if a company does business in multiple states, an LLC may get tricky because LLCs are governed differently in different states.

The right structure for your company

Building a company from the ground up involves making many decisions. To avoid choosing the wrong business structure, educate yourself on the advantages and disadvantages of each. But keep in mind that we've only skimmed the surface. Talk to your tax and legal advisors about which structure is right for your company. ♦

Tax tips to consider before 2009 ends

When it comes to tax planning, there's no time like the present. As 2009 draws to a close, consider these tips now so you're well prepared — at least tax-wise — for 2010:

Maximize your retirement account contributions. It's tax smart to fund your retirement accounts up to the 2009 limits. Why? Because making the maximum contributions reduces your adjusted gross income, thus lowering your taxable income. You can make pretax contributions of up to \$16,500 (\$22,000 if you're age 50 or older) to your 401(k), but they must be made by Dec. 31 to reduce your 2009 income. If you have a traditional IRA, you may be able to enjoy tax-deductible contributions of up to \$5,000 (\$6,000 if you're age 50 or older). And you have until April 15, 2010, to do so and still deduct that amount on your 2009 tax return.

Review your investments. It likely has been a challenging year for your investment portfolio, what with an up and down stock market. If you're facing capital losses, keep in mind that they'll affect your 2009 tax bill only if you recognize the loss by selling the investments this year.

To determine your capital gains liability for the year, your realized capital losses are netted against your realized capital gains. If your net losses exceed your net gains, you may deduct only \$3,000 of losses per year against ordinary income, such as from salary or interest. Although excess losses can be carried forward to offset capital gains or ordinary income in future years, be aware that it could take a long time to absorb a large loss.

Thus it may be wise to reconsider selling an investment at a loss if you might not have enough gains this year to offset it. Also keep in mind that, even if you do have enough gains to offset losses on investments that are currently losing money, you may be better off riding out the downturn and holding on to those investments until they recover their lost value.

Purchase a car or computer and save taxes. If you're deciding on whether to purchase a new car, light truck, motorcycle or motor home before year end, be sure to consider the new deduction for state and local sales or excise taxes you may qualify for. This deduction is limited to the tax on the first \$49,500 of a vehicle's purchase price and starts to phase out when a person's adjusted gross income reaches \$125,000 (\$250,000 for joint filers).

Are you paying your child's college expenses with a 529 plan? If so, you're able to take tax-free withdrawals to pay for the student's computer and Internet access through 2010.