THE

ADVISOR

conquer the complex

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Thank you to everyone who attended our 2020 Market Outlook! Still have questions about where the Market is going this year? Let's talk.

Donor Advised Funds
Your Charitable Giving Options Abound

Donor Advised Funds (DAF) seem to be the latest craze in charitable giving and their accelerated rise may lead some to believe they are a new opportunity. However, according to the National Philanthropic Trust, the first DAF was created in the 1930's and their regulatory recognition began with the Tax Reform Act of 1969. So if a tool that has been around for this long, why is its popularity growing in recent years?

I would suggest the Tax Cuts and Jobs Act of 2017 has played a significant role. Which begs the question: Should taxpayers consider the use of a DAF in their own circumstances?

As with all financial planning topics, it depends. You may recall in our year-end edition of "The Advisor", YHB Principal Elaine Cain, CPA provided a brief perspective on considering a DAF as part of your tax planning. I'd like to go a bit deeper so that you have a broader picture of how the utilization of a DAF is possible and, after a thorough conversation with your tax and investment advisors, why you may consider them yourself.

A DAF is a fund that you may contribute cash, stock or other investments into and receive a charitable deduction just as if you gave the gift directly to a charity (contributions to a DAF are subject to the same IRS limitations as donations made directly to a charity). However, here's where a DAF may provide an advantage over a gift direct to a charity.

- Perhaps you don't know which charitable organization you want to provide a gift to.
- Perhaps you do have a charitable organization in mind but don't have cash sufficient to meet the gift you desire to give.
- Perhaps you want to group your deductions to maximize the income tax savings without creating a timing or budgeting issue for your charitable organization.

Again, in any of the above circumstances, utilizing a DAF allows you to gift cash or other investments directly to the DAF then distribute funds to charity. Let's go through the scenarios:

In the example where you may not know the charitable organization you wish to donate to, setting up a DAF allows you to make your gift and decide the charity or charities later. You report the charitable deduction on your tax return the same year you fund DAF. Then, these monies can be invested with the potential for growth and future disbursements to charitable organizations of your choice.

It is important to note two things. First, once the DAF has been funded, the control of the investment is at the sole discretion of the fund advisor. This means that you are giving up control over "how" to invest the monies once they are placed into the fund. Second, these monies grow tax free and you may be able to grow your gifts.

There are particulars when it comes to the types of investments that are allowed in DAFs, depending on account thresholds. In general, the larger the DAF the more investment vehicles the advisor of the DAF has to choose from. Remember that you as the donor cede investment control to the advisor of the DAF, but you do get to maintain control over the destination (charity) of the funds.

In the second example, perhaps you have stock to gift to a charity and the charitable organization cannot receive stock as a gift (selling appreciated stock that triggers capital gain tax can be avoided by donating the stock to the DAF).

By donating the stock to the DAF taxpayers are able to maximize gifts to charity as well as limit the tax burden. I like to call this a win-win scenario, but we always need to make sure it works for our circumstances.

Remember, the distribution of the funds to the charitable organization still occurs at your discretion while having no bearing upon your tax circumstance since taxpayers get the tax deduction (subject to IRS limits) in the year the DAF was funded regardless of when the funds get disbursed to charity. If there are still monies in the DAF after you pass away, your heirs may then distribute at their discretion. This now becomes a legacy tool in passing on the DAF to generations that follow, while also reducing potential estate tax.

Another strategic way to utilize a DAF is to bundle charitable contributions. This maximizes itemized deductions in one year while taking advantage of the standard deduction the next. This could work as follows:

Historical Giving	Year 1	Year 2
Charitable Contributions	$ 13,000	$ 13,000
Total Itemized Deductions	$ 23,000	$ 23,000
Standard Deduction	$ 24,000	$ 24,400

$48,400 Cumulative Tax Deduction

Bundled Giving	Year 1	Year 2
Charitable Contributions	$ 26,000	$ 0
Total Itemized Deductions	$ 36,000	$ 10,000
Standard Deduction	$ 24,000	$ 24,400

$60,000 Cumulative Tax Deduction

Bundling charitable deductions creates almost $12,000 more in tax deductions while distributing the same amount to charities at the donor's discretion.

Note: Above example assumes a married filing joint taxpayer filing in 2018 and 2019, not subject to IRS limitations.

One last example of when to consider a DAF is in a year with a large financial windfall. This could be a good planning vehicle to help mitigate tax burden. We don't make decisions exclusively for tax purposes, but without question we consider all factors when making our financial decisions.

Again I cannot emphasize enough that this is something you certainly run through both your accountant and financial advisor. Is there a more perfect scenario than having both of those individuals under one roof, here at YHB? I submit that there is not. Let's chat about how you might be able to incorporate this gifting strategy into your personal circumstances!

JT TRIMBLE

MONETIZING YOUR BUSINE$$

Why do I need to do succession planning? It could be as simple as controlling your own destiny, ask yourself the following questions:

- How would the business continue if something happened to me?
- Would there be an orderly transition of the business?
- Would our client/customer needs continue to be met in a timely fashion?
- How would the business be liquidated?

When evaluating the first question above, be sure to consider the potential death, disability or other personal factors, not just for yourself, but for your entire management team and any other key personnel. You may have been the founder, and/or sole shareholder of the company, but the successes of your business was most likely the result of a team of highly qualified personnel. Addressing one's potential demise or disability is difficult, but considering it while you are healthy will help reduce your anxieties about what the future might hold.

For the business to continue, make sure you provide for installation of stable and solid management during the transition period. A common goal amongst transferors and transferees is to make sure any change is seamless to their customer base. Whether they are seeking a product or a professional service, customers have needs and those needs must be satisfied without major disruption.

Consider having a professional business valuation prepared for your business. This should assist you with developing a range of values to reasonably expect when you begin to actively market the business. Valuations are prepared for many different reasons, so be certain to discuss your purpose with the valuation company. (Learn more at YHBcpa.com/services/business-valuation) Valuation methodologies vary as well, so consider their anticipated approach in your specific situation. A well-documented valuation report can be a valuable negotiating tool in justifying your asking price.

Timing is everything, as most businesses have a life cycle. They have an inception, a stage where they cannot support themselves (i.e. startup phase), they may then have a period of rapid growth, then maturity, and finally, termination. The segments of the life cycle can be influenced by new management, new sources of capital and new services or products. Identifying where your company is in its life cycle is important to your valuation team.

Look for ways of enhancing the overall value and appeal of your business, such as getting your accounting house in order and discussing all relevant legal matters. The due diligence process conducted by potential purchasers and their representatives will include a close examination of your accounting and legal matters.

Tips for Getting your Accounting House in Order:

- Maintain a good environment for internal controls – an accounting system that safeguards your assets is an essential business tool
- Be prudent in regularly preparing financial statements with proper cutoff – this shows potential purchasers that you cared about your financial information
- Promote efficiency in processing transactions
- Take good care of your human assets (employees!)

Legal Considerations:

- Governance – make sure your corporate minute book, articles of incorporation, bylaws and/or operating agreements are in good order
- Ownership agreements – make sure your ownership agreements, buyout documents, etc. are well written and understood by all parties
- Customer and supplier agreements should be accessible and include specific terms with specific time frames
- Lease agreements – all lease agreements should be in writing and current, with no defaults or unexpired terms
- Intellectual Property Protection – any patents, copyrights, or employee assignments should be secured
- Key employee agreements should be in place with incentives and/or non-compete agreements where needed

Be sure to seek legal counsel to get a professional opinion on the items above, and any other recommendations they may have from the legal side.

Potential Sale Strategies:
Most owners have three potential exit strategies as their business matures: internal sale, outside sale; or no sale.

Internal Sale – It is important to choose the right individual and to structure the transaction appropriately. This buyer is typically motivated to perform and supports a smoother transition of the business.

External Sale – Sales to an outside third party typically take longer to come to fruition. You and your professional advisory team will have to analyze the financial and tax aspects of an asset sale vs. a stock sale, and work with the potential buyer and his or her advisory team to achieve your desired results. This strategy will often involve more due diligence from the buyer's side.

No Sale – Make sure you allow for the unknowns and the possibility that your business may not sell. Even the best succession plans sometimes fall through.

Pre-Transaction Planning & Preparation:
Careful consideration should be given to the structure of your potential sale. There are vast differences in the income tax effects between the sale of an asset inside your C corporation compared to one that is held by you individually.

Tom Moler, CPA

Pre-Transaction Planning & Preparation

Gain & Income Tax Implications
Assets Held in C Corporation (Fed 21%, VA 6%)
Gain & Tax Allocated to:

	Gain	Tax Rates Fed + VA	Corporate	Personal	Total
Building ($1,000,000 - $100,000 basis - $100,000 selling expense)	$800,000	27.00%	$216,000	0	$216,000
Liquidating Dividend ($900,000 -$216,000)	$684,000	25.75%	0	$176,130	$176,130
			$216,000	$176,130	$392,130

Building Held by Individual (Fed 20%, VA 5.75%)
Gain & Tax Allocated to:

	Gain	Tax Rates Fed + VA	Corporate	Personal	Total
Building	$800,000	25.75%	$0	$206,000	$206,000

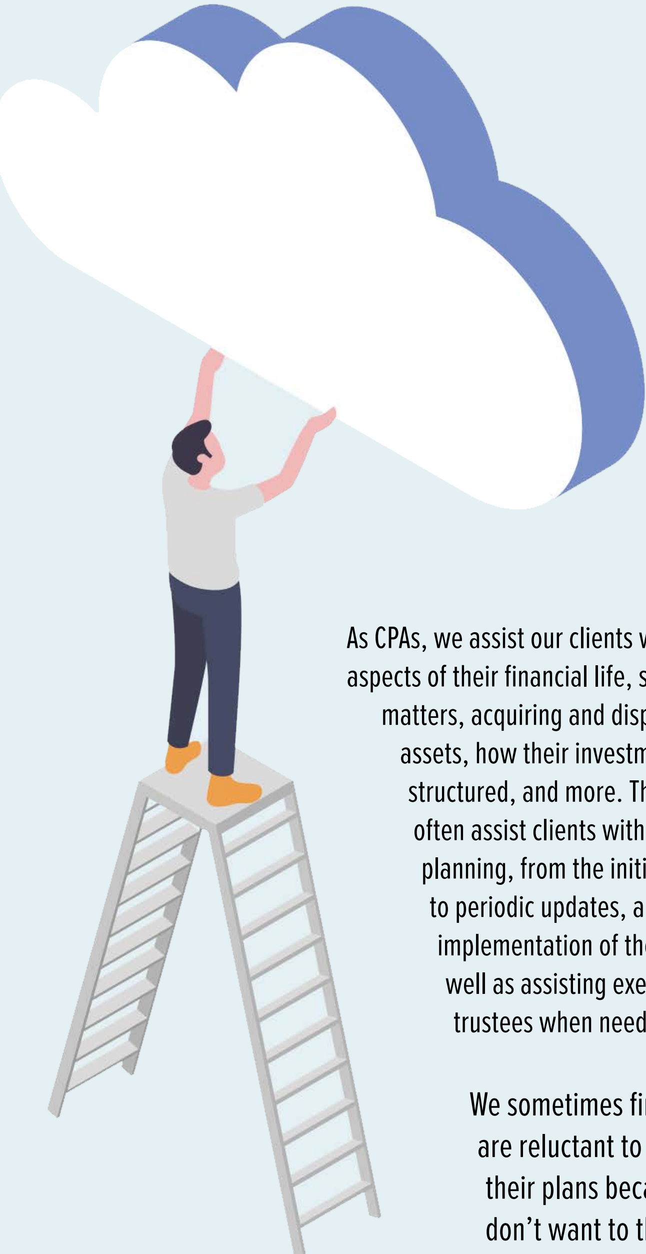
Corporate vs. Individual Sale

Forecasted Cash Summary

	Sale By Corporation			Sale by Individual
	Corporate	Personal	Total	
Cash from Sale	$1,000,000	$0	$1,000,000	$1,000,000
Less: Selling Expense (assumed 10% commission)	(100,000)	0	(100,000)	(100,000)
Liquidating Dividend	(684,000)	684,000	0	0
Less: Estimated Income Taxes	(216,000)	(176,130)	(392,130)	$206,000
Estimated Cash from Sale (After Tax)	$0	$507,870	$507,870	$694,000
Cash Savings				$186,130

Be sure to properly evaluate the entity level of each component of your transaction, and discuss the current income tax rates with your tax team. Share your calculations with your investment advisory team as early as you can in the process.

There are a lot of resources available on succession planning matters. In many cases, your business may have been your life's work, so put your best foot forward to get it across the finish line. If you would like to hear more about how to develop your own customized plan, please contact YHB Principal Tom Moler by email at tom.moler@yhbcpa.com or by phone at 703-777-7739.



I know I need to work on my estate plan... but...

As CPAs, we assist our clients with many aspects of their financial life, such as tax matters, acquiring and disposing of assets, how their investments are structured, and more. Therefore, we often assist clients with their estate planning, from the initial planning, to periodic updates, and the implementation of the plan, as well as assisting executors and trustees when needed.

We sometimes find clients are reluctant to deal with their plans because they don't want to think about their ultimate demise. I'm reminded of the client I worked closely with for many years who, when I mentioned estate planning, said "You don't think I'm going to die, do you?" That worked for him for a number of years, but ultimately caught up to him. Fortunately, he did have a plan in place when he passed.

We often hear, "Yeah, I know I need to work on my estate plan..... but I have no idea who to name as my executor/trustee....." While this is an important decision, do not let this decision stall the process.

Determining whom to appoint as an executor or trustee can be one of the most difficult decisions our clients have to make as they work with their estate plan. It is often easy to decide who is to benefit, but deciding who is going to administer an estate or trust presents a problem.

Many clients are under the impression that their executor or trustee has to be an individual or institution who frequently serves in that role, such as an attorney, a bank trust department, a CPA, or some other businessperson who is familiar with the role of serving as a fiduciary. While this can be the case, it is not a requirement. Many clients have close relatives or a close friend with whom they'd have great comfort asking them to serve in a fiduciary capacity, except the person they have in mind has never served in that capacity before. Because of that, they automatically dismiss the thought of that person serving as a fiduciary. But, do not discount a potential individual only because they've never served in this role before.

A case where someone has a close relative or friend who could serve as their fiduciary, but who doesn't have the expertise, is where your professional advisors can step in and assist. The trusted family member or friend does not have to have the knowledge; they just have to know where to turn for assistance. The key is to surround your fiduciary with a team of advisors to guide them through the process.

We have had many, many cases through the years where we've worked with a client during their lifetime and then, after they've passed, we've continued to work with their named fiduciary to assist in administering an estate or trust. We'll often work alongside the client's attorney, investment advisor, and other advisors in administering the estate or trust. It's often the same team of advisors assisting the fiduciary, which assisted the client who passed away or established the trust.

As you work with establishing or updating your estate plan, please remember that the members of YHB's Family Legacy Services Team have significant experience in assisting both clients and their fiduciaries with their tax and accounting needs. Don't hesitate to contact us if you'd like more information or want to discuss this further.

Greg Crawford, CPA

FAFSA: Some Do's and Don'ts

Just as I did my senior year of high school, and every subsequent year through graduate school, many students and parents will find themselves filling out the Free Application for Federal Student Aid (FAFSA). In addition to providing assistance in registering for the selective service this is the only application to apply for aid from the Federal government when attending college. This aid includes several grants, federal work-study, various loans, and other scholarships. However, many college financial aid departments still require a completion of the FAFSA even when a student is offered merit based aid, without need for further assistance, from the college itself. The FAFSA certainly creates uncertainty for students and parents with seemingly straightforward circumstances, but an even bigger one for those who have a few added details to consider. Let's look at some common questions and hopefully some answers to help navigate filing the FAFSA and some items for consideration when you're able to plan ahead.

Who fills it out and what do you need?

Students heading to college are generally required to file the FAFSA, which then means parents of the student are also required to fill out their portion of the FAFSA. Students should have their SSN, Driver's License, tax/income records, and create an FSA ID. Parents will need their prior-prior year income tax return (your 2018 tax return for the 2020-2021 school year); information on cash such as checking, savings, investment accounts, pre-paid tuition plans, investment real estate, and business assets; and untaxed income records such as child support, interest income, etc. This also brings up the question of which parent should file the FAFSA, for instances when parents of the child have separated. In these circumstances, the parent with whom the child lives the majority of the year (deemed the custodial parent) should fill out the form. Under the unique circumstance where a child spends equally 50% of their time in each household, the parent who provides the majority of the financial support for the child should file. It's important to note that colleges can and will verify a copy of the divorce decree to verify FAFSA filing responsibilities as well as child support.

If a student will benefit from a 529 account owned by their grandparent (or possibly non-custodial parent). Does this need to be included on the FAFSA?

I encourage having the entire family can be involved in planning for college, but it certainly adds a layer of complexity when filing the FAFSA. It's also important to distinguish between account owner and account custodian. For example, I can open a 529 account for my son and I am the account owner while he is the beneficiary. However, let's say I have been contributing to an UGMA/UTMA account and, after a few years, convert it into a 529. Since my son is still a minor when I convert it, I am the custodian of the account while my son in the owner. In this circumstance my son would have to report the 529 on his FAFSA. Pertaining to our question, because this is not a student or custodial parent owned asset, this might be able to be left off of the FAFSA as an asset. If the grandparent owns the account and the student is simply a beneficiary, it will not need to be included as an asset. Keep in mind that once the student takes a distribution from the account, even if it is a qualified distribution, the student will need to claim the distribution as untaxed income on their FAFSA. Note that this may have a big impact on their aid eligibility. This circumstance provides a unique planning opportunity for the use of 529 accounts and college funding; something to get your financial advisor and tax accountant's perspectives on if they have familiarity with the FAFSA

Which years do the students and parents need to file the FAFSA?

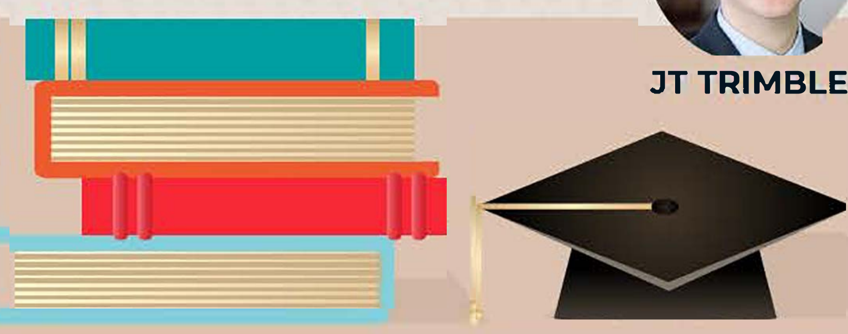
For students, every year that they are going to college or post-graduate school they will need to file the FAFSA. Thus if a student intends on attending college or graduate school in the fall of 2020, they must complete the 2020-21 FAFSA. For parents this is a bit more of a nuanced answer. If the child is a dependent undergraduate student, then you must file a FAFSA along with your dependent student. If the student may qualify as an independent student, then only the student must file the FAFSA and parents are off the hook. Independent students include those who are married, age 24, a veteran, homeless, a graduate student, or provide a degree of support for dependents or children. The latter (independent student) is sometimes a bit of an exercise to identify accurately but you may go through a questionnaire on the FAFSA website. It's important for the student, and parent, to identify the dependency status accurately.

What's the big deal? It's not like we will get any aid anyway.

This is a common response that I received both as an Enrollment Counselor for a private university and frankly had myself as a student during undergraduate and graduate school. Honestly, it may be correct. However, there are plenty of options that do rely on the FAFSA that may not be considered in this response. For example, work-study is not "free" aid as the student is required to work in order to receive the aid, but it is aid nonetheless. Furthermore, colleges do not have unlimited opportunities for students desiring to fulfill their work-study aid and these opportunities are often provided to currently/previously enrolled students before those about to enroll. If your student has already firmly decided where they plan on attending it is definitely a good idea to reach out to the financial aid department to see if they are eligible to receive work-study as a part of their aid package. If they are eligible, then my next advice would be to ask both the financial aid and admission offices if they are able to refer you to any department on campus that has work study available. Sometimes this may be an internal student job board that you're only able to see upon enrolling. Often, as an incoming freshman, you take what you can get; but sometimes you're able to work in a department that you have interest in such as Athletics, Student Activities, Residence Life, Campus Recreation, Academic Advising, and others.

The FAFSA can certainly be a bit of bear to tackle but it's often more beneficial than we realize. Even if the aid is minimal, every little bit helps! My last word of advice is to be very skeptical of anyone offering to fill out the FAFSA for you, for a fee. First of all, the FAFSA is FREE to file so paying for it is already ill-advised; this is not a tax return. Secondly, going to a financial planner, years ahead of time, will help you incredibly more than paying someone to file the FAFSA for you, as your student is about to enter college. Finally, you know your circumstances far more than anyone you will pay to do this for you. Better to plan ahead, as a part of your overall financial plan, than to scramble at the last minute and use your hard earned money on something that is free to begin with.

JT TRIMBLE



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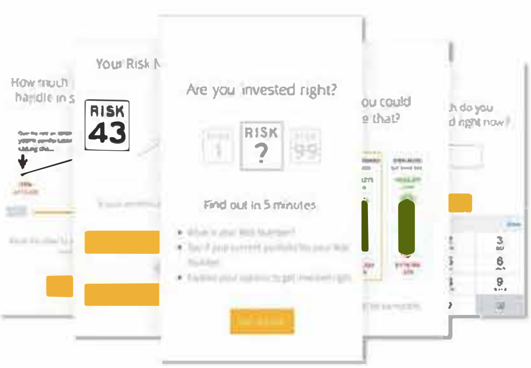
What is your Risk Tolerance?



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