

Fall 2018

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How to get a handle on employment churn

If you have ever lost a key employee, you know the immediate and long-term hit to your bottom line. With the markedly low current unemployment rate, finding new hires in this job market may be harder than ever. Luckily, there are steps you can take to reduce employee churn and the challenges it brings. Here are a few to consider:



■ Review employee compensation.

Do your homework to ensure your company is offering competitive industry salaries and benefits for your area. Consider making pay adjustments to key employees that would be hard to replace.

Also, review benefit packages. Many of your competitors may be offering additional vacation, enhanced family leave and other benefits. A good way to look at this additional expense is to balance the additional cost against the cost of replacing one or two key employees.

■ **Talk with employees about what keeps them satisfied.** A 2015 IBM workplace study found that the priorities of employees across working generations align on major job-related issues, including fair treatment, growth opportunities, flexible work hours and positive impact of their work.

During performance reviews, ask your employees about their priorities. This will give you insight into what

retention strategies are working well at your company, or tip you off on why employees may end up leaving. Anonymous surveys may also be an effective way to gauge the satisfaction of your employees.

■ **Offer career paths to employees who want them.** Chances are if employees feel stuck in their job roles they will go looking for opportunity elsewhere. Show the ambitious employees at your company that their desires for career development are heard by offering them more responsibility and trust in their roles. This could come in the form of additional assignments outside of their usual scope, plus more autonomy.

■ Cross-train employees in key functions.

This not only offers employees new challenges and a chance to develop more skills, it also provides you with the comfort of knowing that key positions can be temporarily backfilled should someone leave unexpectedly. >

And if you need to hire new employees...

You may be able to increase your candidate pool (and tax breaks) by considering individuals who are a part of Work Opportunity Tax Credit (WOTC) target groups. This federal tax credit is available to employers who hire and retain veterans and individuals the government identifies as having major barriers to employment, including those receiving:

- Long-term unemployment
- Temporary Assistance for Needy Families (TANF)
- Supplemental Security Income (SSI)
- Long-term family assistance
- Food stamps

Other WOTC target groups include designated community residents living in empowerment zones or rural renewal counties, vocational rehabilitation referrals and individuals who were incarcerated. With the WOTC, you may be able to claim up to \$2,400 for each employee who works 400 or more hours in their first year. >

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IRSTAX NOTES

Natural disaster scams peak during hurricane season

Beware of more charity scams during this year's hurricane season, now through Nov. 30. Criminals often take advantage of people who want to help natural disaster victims. The most common ways scammers will try to collect money and personal information is by pretending to be a member of a charity or by creating a fake charity website.

Some scammers even pretend to work for the IRS to get natural disaster victims to work with them to file casualty loss claims. They use that relationship to steal the victims' tax refunds.

If you would like to make a donation to a charity that supports hurricane or other natural disaster victims, use the IRS Tax Exempt Organization search tool to find a legitimate charity.

No change to third-quarter interest rates

The third-quarter interest rates on overpayments are 5 percent for individuals and 4 percent for corporations. Corporate overpayments exceeding \$10,000 have a 2.5 percent interest rate. The rate charged on underpayments is 5 percent. And large corporate underpayments are charged 7 percent.

Do not wait to renew your ITIN

Renew your Individual Taxpayer Identification Number (ITIN) soon if it is set to expire at the end of 2018. The IRS wants taxpayers to submit their renewal applications as soon as they can to beat the last-minute rush and avoid refund delays next year.

Taxpayers who will need to file a tax return in 2019 and have ITINs that are expiring will need to submit a renewal application. ITINs with the middle digits 73, 74, 75, 76, 77, 81 or 82 need to be renewed even if you have not used it in the last three years. ➤

How much should you pay yourself?

One of the biggest upsides of having your own business is flexibility. But without discipline and a strategically devised plan, business owners can get into serious financial trouble. Employees in larger firms often rely on the human resources department to establish pay scales, retirement plans and health insurance policies. In a small company, all those choices (and many more) fall to the owner, including decisions about personal compensation.



While there is not a one-size-fits-all formula for determining how much to pay yourself as a business owner, here are three factors to consider:

■ **Determine your business and personal expense needs.** Conducting this exercise lets you know how much salary you can realistically draw without hurting profitability.

Start with your household budget, then determine how much you are willing to draw from personal savings to keep your household afloat as the company grows. For startups, owner compensation may be minimal. However, going too long without paying yourself a reasonable salary is not sustainable.

Be prepared to prove that you are in business to make a profit; otherwise the IRS may view your continuously unprofitable business as a hobby – a shell enterprise aimed at avoiding taxes.

■ **Know the market.** Ask yourself: If you were working for someone else, what would they pay for your skills and knowledge? Once you have thought about it, discuss salary levels with small business groups and colleagues in your geographic area and industry and see if you are in the ballpark.

Use the Department of Labor and Small Business Administration websites as additional resources to determine your salary. In the early stages of your business, you probably will not draw a salary that is proportional with the higher range of salaries, but at least you will learn what is reasonable.

■ **Figure out what you can afford.** Review and continually update your firm's cash flow projections to determine the salary level you can reasonably sustain while keeping the business profitable. As the company grows, that level can be adjusted.

The IRS is focusing on businesses that do not appear to be paying a reasonable salary in an effort to avoid paying employment taxes. There is little to be gained by spending time fighting the IRS in this area.

For assistance with this issue or other business concerns, contact our office. ➤

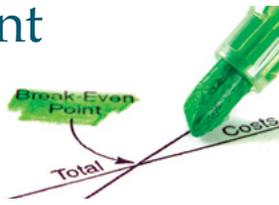
Big sales tax changes for businesses?

In a decision handed down this year in South Dakota vs. Wayfair (an online furniture retailer), the U.S. Supreme Court ruled that South Dakota can require Wayfair to collect sales tax even though it does not have a physical presence in the state. In this case, the court ruled that "economic presence" is sufficient to create nexus.



The impact of this ruling is up for debate and will vary by state. For instance, South Dakota does not have individual income taxes, and businesses with less than 200 orders or \$100,000 in sales are exempt from this economic presence rule. ➤

Know your breakeven point for business success



Whether you are starting a new business, expanding current operations, contemplating an acquisition or downsizing, you should know your company's current breakeven point. Why? Because the health of your business depends on it.

The breakeven point

Breakeven is simply the point at which all your costs equal income – no profit, no loss. It is an excellent starting point for finding out where the business is and where it can go. It is not only the first step in planning future growth, it can show how much sales volume is needed to cover fixed and variable expenses. Once a business hits the breakeven point, all gross profit beyond that point can go directly to improving the bottom line.

Calculate your breakeven point

Breakeven is relatively easy to understand and use. Here are steps on how to find your company's breakeven point:

1. Review your annual financial statement. Your focus is to understand what costs are fixed and what costs are variable or semi-variable.

Fixed expenses are those that do not generally vary in relation to sales volume. For example, rent, depreciation, utilities and insurance usually stay constant. Variable expenses are typically the cost of goods sold and other costs of sales, such as direct labor and sales commissions. Keep in mind, some costs are part fixed and part variable. You will need to use your judgment to split these items into reasonable proportions.

2. Calculate your gross profit margin percentage. Knowing selling price and variable costs allows you to compute your gross profit margin percentage.

First, add up your costs of goods and services sold for the year. Then take that number and subtract it from your total revenue to get your gross profit dollar amount. Then calculate your gross profit margin percentage by dividing the gross profit by your revenue.

For example, assume your business's total revenue is \$120,000 so far this year. Assume the total cost of goods and services is \$90,000. Your gross profit margin percentage is 25 percent ($\$120,000 - \$90,000 = \$30,000 \div \$120,000 = 25$ percent).

3. Determine your breakeven point. Divide your fixed costs by your gross profit margin percentage to arrive at breakeven. So if you have fixed costs of \$10,000 and your gross profit margin percentage is 25 percent, your breakeven point is sales of \$40,000 ($\$10,000 \div 25$ percent = \$40,000).

Once you have determined your business's breakeven point, you will have a good sense of whether or not you are charging enough for goods and services to cover how much it takes to make and provide them. Higher breakeven points typically go hand-in-hand with higher fixed costs, which means you will need to sell more. Keep in mind there are certain limitations for the use of breakeven analysis. It ignores the importance of cash flow and makes the assumption that fixed and variable expenses will stay within the parameters used to calculate the breakeven point. ➤

Keep your cash flow on track all year long

The No. 1 cause of business failure is poor cash flow management.

Cash fluctuates in every business. If seasonal ebbs and flows are anticipated and managed well, you can continue to operate without undue concern. But failure to actively manage cash flow has landed more than a few small businesses in bankruptcy. Here are four suggestions for monitoring and managing cash flow throughout the year:

1. Analyze and track. It is hard to fix something if you do not know it is broken. Prepare schedules that track each month's cash balance. Start with the beginning balance, then add receipts (from collections and asset dispositions, for example), subtract outflows (to purchase inventory, make payroll, cover utilities, etc.), and calculate the ending cash balance. Use this analysis over several business cycles to develop a realistic cash flow forecast.

2. Set good credit policies. If you are accepting new customers, ask for references. Determine whether they are likely to pay on time – before extending credit. Send out invoices the same day goods are shipped, and follow up when payments are even a day late. If you need to, adjust payment and credit terms. You could also offer percentage discounts for early payers or require milestone payments for longer projects. Generate accounts receivable aging reports to help you manage your receivables and help identify exactly who is falling behind on payments.

3. Decelerate disbursements. Separate payments into three categories:

- Must pay (payroll, taxes, utility bills)
- Important to pay (payments that offer a reasonable grace period)
- Flexible financing (some suppliers may work with you to schedule regular payments)

These categories will help you manage disbursements so you can pay vendors on time – not too early, not too late.

4. Grow cautiously. Take care when expanding into new markets, developing new product lines, hiring employees, or ramping up your marketing budget. All require cash. Do not travel too far down that road before generating accurate cash forecasts. And always ask for expert help when needed.

If you have tax or accounting-related questions about your business's cash flow, do not hesitate to call. ➤

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Make managing obsolete inventory a priority

Chances are most warehouses have inventory coated with a thick layer of dust. What is important isn't whether or not obsolete inventory exists, but how to keep it from costing your business big bucks.

■ **How inventory becomes obsolete.** There are many reasons why inventory may become obsolete. Alternative products may arrive in the marketplace at lower costs to the consumer. And technological advances are often a double-edged sword. Changes in product features will often adversely affect the value of your existing inventory.

■ **The effects of obsolete inventory.** Carrying obsolete products in your warehouse or retail store tends to increase operating costs without generating profit.

In addition, your financial reports may overstate business assets, especially if inventory is a major item on your balance sheet. Even your tax bill may be affected. Failing to recognize the expense of obsolete inventory may overstate net income.

■ **How can you reduce the cost of excess inventory?** Consider these tips to help you keep ahead of obsolete inventory:

■ **Define "obsolescence" for your product lines ... and then be proactive.** Using recent sales data, calculate how many months of inventory you have on hand. Create a report that shows inventory that has excess months of cover. If an item has not sold in a certain number of months, start moving that item by offering sales discounts.

■ **Write off products that are unlikely to generate profit.** It is a better financial strategy to write off a little each year then to wait and have a huge write-off in one year.

■ **Establish a regular schedule for reviewing inventory.** Counting goods at the end of the year is usually not enough to manage obsolete inventory. Make inventory review a quarterly, if not monthly, process.

■ **Manage and plan inventory.** There is nothing wrong with timing inventory write-offs as part of tax planning. As long as the approach is reasonable and consistently applied, it can be a great tool to manage tax obligation.

Please call if you have questions about how your obsolete inventory may affect your business taxes. >

Calendar

OCTOBER 15

Filing deadline for 2017 individual tax returns on automatic six-month extensions of the April due date.

Filing deadline for 2017 calendar-year tax returns for C corporations with extensions of the April due date.

DURING NOVEMBER

Estimate your 2019 income tax liability and review your options for minimizing your 2018 taxes. Call to schedule a tax planning review. >