

January 31, 2012

ALERT: Changes in business environment require re-evaluation of tax strategies

Businesses, tax laws and the economic environment are constantly evolving – and any change could mean that tax strategies once not applicable for you may now offer significant benefits. Your AGH team considers tax-saving ideas when working with you, but may not be aware of all the changes in your business which could trigger increased potential benefit.

If your company is involved in any of the following events/activities, you may be eligible for a related tax-minimization strategy, and we can help you evaluate whether the potential benefits outweigh costs – as is typically true. For more specific information on how this could apply to your situation, please contact your AGH tax professional.

- **Development of new or revised processes or products, especially for manufacturing entities:** If your company develops new products or processes, it's very likely you have expenses qualifying for the **research and development tax credit** – especially in a manufacturing environment. Typically, expenses can be deducted from taxable income, but those qualifying as research and development may also earn a tax credit. This can result in substantial tax savings simply by putting a system into place to identify and track qualifying research costs, such as wages, supplies and contracted development expenses. Tax benefits continue every year for which you have qualifying expenses. *NOTE: The tax provision allowing R&D credits has expired but we expect it to be extended again, as it has been the past few years.*
- **Purchase, renovation or construction of a facility within the past 10 years:** Any of these activities may result in tax benefits from performing a **cost segregation study**. Facilities are typically depreciated over periods up to 39 years; however, personal property components of the facility can be identified and “carved out” of the total project to benefit from accelerated depreciation over shorter periods, which results in lower taxes and improved cash flow. For major building or renovation projects, it's common to be able to accelerate depreciation for 15-25% of the total project cost. Even better, if projects occurred within the past 10 years and accelerated depreciation has not been used for qualifying personal property, a “catch-up” deduction may also be available.
- **Any international transactions, exports or other international activity:** Businesses which export goods or services, make payments to foreign companies or foreign persons, participate or have ownership in foreign ventures, maintain foreign bank or securities accounts, have US income tax compliance reporting requirements associated with those activities. Failure to fulfill these reporting requirements can result in significant penalties, most of which start at \$10,000 per occurrence. Protect your profits and minimize the risk of unnecessary penalties by conducting an international activities compliance review.

- **Significant export activity:** Companies with substantial sales of US-sourced products outside the US can take advantage of the difference in tax rates on ordinary income (with a top rate of 35%) and qualified dividends (taxed at 15%). By setting up a related entity called an **Interest Charge Domestic International Sales Corporation (IC-DISC)**, companies pay a commission for export sales through the new entity, and receive the commission back as qualified dividends. The IC-DISC can deliver up to a 20% tax rate savings as long as qualified dividend tax rates remain at 15%.
- **Sales, operations, warehousing or transportation activities conducted in multiple states:** Businesses which conduct transactions, locate staff or facilities, or even deliver products in multiple states may be subject to income tax in those states. As states become increasingly aggressive about tax revenues, almost any presence may generate tax liabilities. A **nexus study** evaluates the nature of activities and operations in each state and seeks to minimize tax liability by strategic location and management of those business activities, which can help companies lower their total state tax bills.
- **Significant rise or fall in the cost of materials or inventory:** Peaks and valleys in materials and inventory costs are a signal to re-evaluate whether the company's **inventory valuation method** is still appropriate. An appropriate inventory valuation method offers both accurate estimation of inventory assets and maximum tax benefits. Companies which have experienced significant inventory cost changes may be able to realize substantial tax savings with little up-front cost.

These and other tax-minimization or profit-improvement strategies may be applicable to your business. We encourage you to discuss any ownership, regulatory, capital improvement or other major changes in your business with your AGH tax professional to see whether new options to benefit you may now be appropriate.

For more information about any of these tax strategies, please contact your AGH tax professional or vice president of tax services Shawn Sullivan at (316) 291-4110 or email shawn.sullivan@aghlc.com.

Note: Pursuant to federal regulations imposed on practitioners who render tax advice ("Circular 230"), we are required to inform you that any discussion of tax matters contained herein is not intended or written to be tax advice, and cannot be relied upon as such, nor can it be used for the purpose of: (i) avoiding tax penalties that may be imposed by the IRS or states, or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein. If you seek definitive tax advice on a matter, please request a written tax memorandum from your AGH tax advisor.