DEANDORTON

DEAN DORTON ALLEN FORD, PLLC

NEWSLETTER

FALL 2016

Inside

Valuation Discounts Under Siege

A popular estate planning technique has involved structuring transfers of ownership interests in family entities holding operating businesses, real estate, or other investments to take advantage of valuation discounts. These discounts have related to the lack of control and marketability inherent in transferred interests.

The Internal Revenue Service recently issued proposed regulations that, if finalized in their present form, will adversely impact the ability of families to transfer assets at discounted values. Hearings on the proposed regulations are scheduled for December 1 of this year, and the regulations may be finalized soon afterward.

If you have been considering a transfer in an existing family entity and have remaining estate and gift tax exemptions, you should consider acting before December to take advantage of available valuation discounts. Establishing new family entities for the same reason may be feasible.

Additional Considerations

In 2016, each individual has a lifetime exemption from gift and estate taxes of $5.45 million. Assets gifted during life are not eligible for a basis step-up at death. So, if your estate is not likely to be taxable, you might be doing your heirs a favor by holding onto your assets until death rather than gifting them during your life.

From a non-tax perspective, the creation and transfer of family limited partnerships and LLCs is not for everyone. Formalities of operation must be observed and additional tax returns normally are required. Further, the gifting of such assets requires giving up both control and beneficial enjoyment, a result that many may find to be undesirable.

Please contact us for more information or to discuss how we can help with your gift and estate planning and with valuation concerns.

Elizabeth Leatherman, eleatherman@deandorton.com

TAX QUOTE

"There is no end, of course, to people promoting the use of the tax code to support nice-sounding things. That's why we have the tax code we do."

– Holman W. Jenkins Jr.

(from a compilation by Jeffrey L. Yablon, a tax attorney with Pillsbury Winthrop Shaw Pittman LLP in Washington)

Just How Complex is Our Federal Tax System?

Ridiculously complex is the answer, according to a recent article from the Tax Foundation (www.bit.ly/2ccoP9r). Americans are spending a record number of hours and dollars to comply with federal tax law.

In the last 60 years, the Internal Revenue Code has increased nearly six-fold, from 409,000 words in 1955 to more than 2.4 million words now. In addition to the Code itself, 7.7 million words of tax regulations have been issued by the IRS over the last century; these regulations generally are used to clarify how the tax statutes should work in practice. Another 60,000+ pages of federal tax-related case law are used by tax accountants and tax attorneys when assisting their clients with complex issues.

Americans will spend more than 8.9 billion hours complying with IRS tax filing requirements in 2016, according to estimates from the Office of Information and Regulatory Affairs. That is equivalent to over 4.2 million people working full-time year round on nothing but federal tax returns. In addition, the article estimates this burden will cost tax-filers $409 billion. The five most-costly types of filings with their respective annual hours burden and annual cost in dollars are:

	Total Annual Hours Burden	Total Annual Cost
U.S. Business Income Tax Returns	2,832,500,000	$147,431,625,000
U.S. Individual Income Tax Returns	2,647,000,000	$98,680,160,000
Income Tax Returns for an S Corporation	889,393,518	$46,292,932,612
Form 4562 – Depreciation and Amortization	448,368,447	$23,337,577,666
Employer's Quarterly Federal Tax Return	388,256,964	$20,208,774,976

Keep in mind that this data is only for federal taxes. State and local governments have their tax filings, which add significantly to the hours and cost of overall tax compliance. While "tax simplification" is talked about often, the opposite has been happening year after year. Unless something drastically changes, be prepared for the time and monetary burden of tax compliance to continue to grow.

Matt Smith, msmith@deandorton.com

Crowdfunding: What Is It and How Is It Taxed?

"Crowdfunding" is the practice of funding a project or activity by raising funds from a large number of people. Crowdfunding has grown dramatically in recent years in part from the formation of websites such as Kickstarter and GoFundMe. In 2015 alone, an estimated $34 billion was raised via crowdfunding. The typical crowdfunding model involves an initiator who proposes a project to be funded, people financially willing to support the idea, and an intermediary who brings the parties together.

For the recipient, whether or not the funds are included in gross income depends on a number of factors. The Internal Revenue Code includes in gross income all income from whatever source derived except as otherwise provided by law. In other words, all income is taxable unless it, by law, is excludable. A recent IRS letter (not representing an official position) provided guidance on the issue of crowdfunding taxability. The letter concluded that crowdfunding receipts generally are includible in income unless they are:

- Loans that are required to be repaid,
- In exchange for an equity interest in an entity, or
- A gift made out of detached and disinterested generosity and not made from a moral or legal duty.

Continued on page 3

Crowdfunding: What Is It and How Is It Taxed? (continued)

In most cases, the issue of taxability is clear. For example, a business that raises funds to expand its operation and offers services at a later date as an incentive with no intention of repaying the funds or without granting an equity interest in the company will include its crowdfunding in taxable income. Some instances require a much more in-depth analysis of the facts and circumstances.

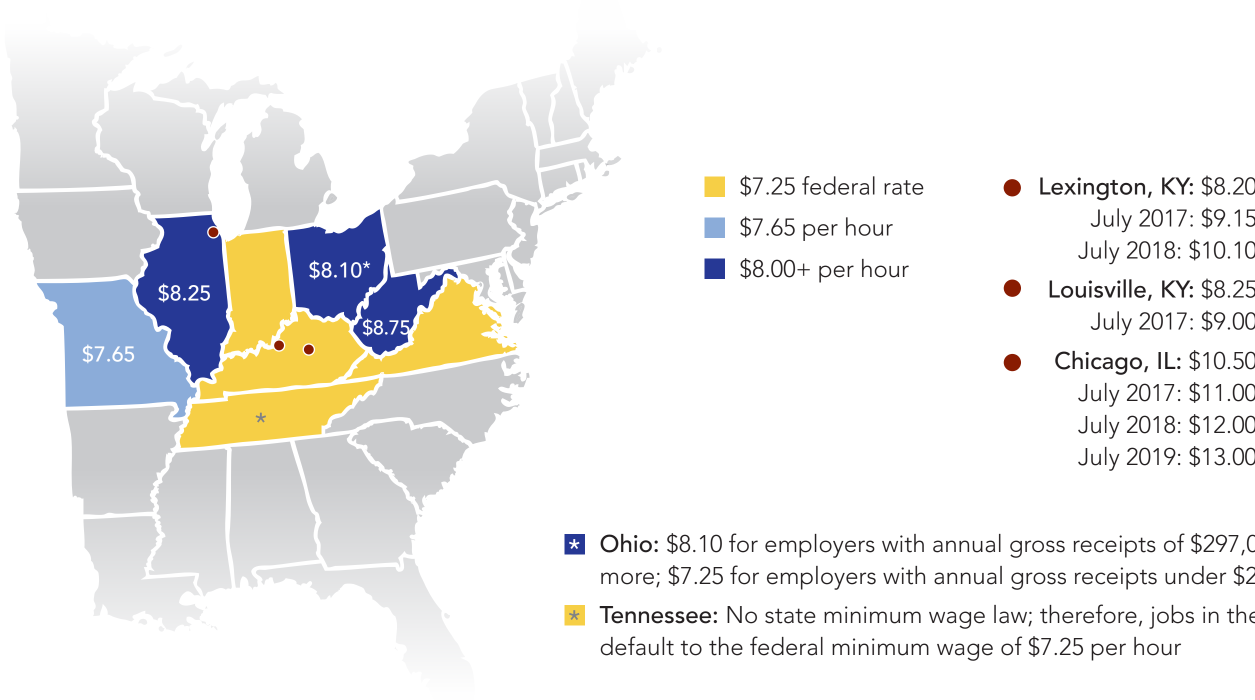
No court cases regarding crowdfunding have been decided, and the IRS has not issued a definitive conclusion on how they will treat crowdfunding.

Adam Campbell, acampbell@deandorton.com

Minimum Wage

In the cities where we have offices, Louisville and Lexington, local governments have established their own minimum wage standards at levels exceeding those of federal and state governments. We thought it might be interesting to see how minimum wage rates differ in states contiguous to Kentucky.

The federal minimum wage is $7.25 per hour. Kentucky generally follows federal, but Louisville has raised its minimum wage to $8.25 and has scheduled an increase to $9.00 in July 2017. Lexington's minimum currently is $8.20, scheduled to increase to $9.15 in July 2017 and $10.10 in July 2018. Illinois, Indiana, Tennessee, and Virginia generally follow federal, but Chicago's minimum is $10.50, scheduled to increase to $11.00 in July 2017. West Virginia's minimum is $8.75 and Missouri's is $7.65. Ohio's minimum is based on each employer's gross receipts, with a threshold of $297,000. Tennessee does not have a state minimum wage law, so jobs in the state default to the federal rate of $7.25.



Ohio: $8.10 for employers with annual gross receipts of $297,000 or more; $7.25 for employers with annual gross receipts under $297,000

Tennessee: No state minimum wage law; therefore, jobs in the state default to the federal minimum wage of $7.25 per hour

Carrie Asalon, casalon@deandorton.com

Employers Beware: Final Employee Overtime Rules Soon Become Effective

Earlier this year, the U.S. Department of Labor (DOL) released final regulations which are designed to make many more employees subject to overtime pay rules. The new rules have the impact of tightening the overtime exemptions for executive, administrative, professional, IT, and outside sales employees. The changes are effective December 1, 2016.

What are the Main Changes?

- *Exempt Salary Threshold* — Under current law, certain executive, administrative, and professional employees are exempt from overtime pay if their salary is at least $455 per week ($23,660 per year) and other criteria are met regarding job roles and responsibilities. In addition to the salary requirement noted above, the respective duties for executive and administrative positions are:
    - Executive: Employee's primary duty must be managing the enterprise (or a department of the enterprise), must regularly direct the work of at least two other full-time employees, and must have the authority to hire or fire employees.
    - Administrative: Employee's primary duty must be the performance of office or other non-manual work related to management or general business of the employer and includes the exercise of discretion and independent judgment.

  Effective December 1, 2016, the exemption from overtime pay for the above positions is applicable only if the employee's salary is at least $913 per week ($47,476 per year). Up to 10% of this salary threshold may include certain bonus or incentive payments (including commissions) that are paid at least quarterly.
- *Automatic Adjustments* — The minimum salary level for these overtime exemptions will increase every three years to match national wage growth. The DOL projects that the minimum salary level will rise to $51,000 on January 1, 2020.

What Has Not Changed?

The DOL did not make changes to the duties tests for executive, administration, or professional exemptions. In addition, no changes were made in the regulation governing how employees are to record or report hours worked. No modifications were made to part-time employees, including those who perform exempt duties on a part-time basis.

Carrie Asalon, casalon@deandorton.com

Cybersecurity: Advice on Protecting Your Information

In our last newsletter, we highlighted some current fraud trends related to electronic fund transfers (read the article at www.deandorton.com/759). Responses we have received make it clear – business owners are concerned about the increased fraud risks caused by our reliance on today's technology and are interested in ways they can educate employees to enhance cybersecurity.

Phishing schemes, which seek to acquire sensitive information for malicious intent, are increasing. Users must maintain caution, protecting usernames, passwords, and credit card and bank account information. Despite widespread media attention to various forms of these schemes, fraudsters continue to successfully manipulate victims, perhaps because a natural human tendency is to trust. We recommend employees be trained to be constantly skeptical, asking questions before opening or responding to suspicious emails. According to the Verizon 2015 Data Breach Investigations Report, 23% of recipients open phishing messages and 11% click on attachments. Half of this group does so within the first hour of receiving the email.

Continued on page 5

Cybersecurity: Advice on Protecting Your Information (continued)

The National Cyber Security Alliance estimates that 41% of targeted attacks are against organizations with fewer than 500 employees. A relatively easy, affordable protection is to install a spam filter, so your employees don't receive as many unwanted emails (this may help productivity, too). Individual users should:

- Be particularly cautious if an email is from an unknown sender. Do NOT click on links, download files, or open attachments.
- Be leery if a request for information is unexpected, especially if it conveys a sense of urgency.
- Never enter personal information onto or copy web addresses or click on links from a pop-up screen.
- Never share passwords!

Employers must recognize that physical security is important. Laptops, hard drives, and flash drives should be encrypted. Computer devices should not be left in vehicles; if they are, they should be hidden. Disposal of obsolete equipment needs to be done with care, after all sensitive information has been removed.

Elizabeth Woodward, ewoodward@deandorton.com

Be glad this wasn't you!

Earlier this summer, the Milwaukee Bucks basketball franchise fell victim to an email phishing scheme. A fraudster impersonating team president Peter Feigin requested, and was given, 2015 Form W-2s for all employees. In addition to annual salary, the Form W-2 discloses each person's name, address, and social security number.

People News

We welcome the following new team members:

Isaac Archer joined our Business Consulting Team in Lexington. He comes from CapinCrouse, a CPA and consulting firm based in Los Angeles, California. Isaac earned his Bachelor of Science degree in Business Administration and Accounting from Asbury University and his Master of Professional Accountancy degree from Azusa Pacific University in Azusa, California.

Adam Campbell, a CPA, joined our Tax Team in Lexington. Adam earned his Bachelor of Business Administration degree in Accounting from Eastern Kentucky University. He has over 10 years of work experience, including stints in public and private industry accounting and in working in thoroughbred racehorse businesses. Adam is active as a board member and officer of Central Kentucky Riding for Hope, and he is a licensed thoroughbred racehorse trainer.

Kyle Fiedler joined our Office Services Team in Lexington. He currently is studying psychology at the University of Kentucky.

Alex Goffner joined our Assurance Services Team in Louisville. He graduated with a Bachelor of Arts degree in Accountancy from Thomas More College and has passed all four sections of the CPA exam. Alex has almost two years of work experience.

Jerald Miles also joined our Assurance Services Team in Louisville. He graduated with a Bachelor of Science degree in Business Administration from the University of Louisville. He has over 15 years of accounting and auditing work experience.

Christi Smith joined our Human Resources Team in Lexington. She has over nine years of work experience. While working, Christi earned an Associate of Arts degree in Business Management at Sullivan University and is on track to earn a Bachelor of Arts degree in Business Management with a focus on Finance at Sullivan by the end of this year.

Gracie Warren, a CPA, joined our Assurance Services Team in Lexington. She comes to us from PricewaterhouseCoopers in Birmingham, Alabama. She earned Bachelor and Master of Business Administration degrees in Accounting from Samford University in Birmingham.

DEANDORTON

DEAN DORTON ALLEN FORD, PLLC

106 West Vine Street • Suite 600 • Lexington, KY 40507

People News, continued

We recognize the following activities and accomplishments of our team members:

Chip Dalton successfully passed the exam necessary to become a Certified Professional Coder.

Payton Miller earned the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control Certificate.

David Richard earned AICPA's Not-for-Profit Certificate I badge.

Scott Layton and **Jessica Ruen** passed all four sections of the CPA exam. Two new hires who are joining us in September, **Cameron Sallee** and **Laban Miller**, also passed all sections of the CPA exam.

Cathryn Allison was elected Treasurer of the Rotaract Club of Lexington.

Nick Lynch spoke on fraud at colleges and universities at the Kentucky Public University Business Officers Conference. **Crissy Fiscus** and **Megan Crane** also spoke at the conference, covering GASB 73, fraud, and the Fair Labor Standards Act.

Missy DeArk, **John Herring**, **Elizabeth Leatherman**, and **Nick Lynch** spoke at the National Business Institute Conference on Divorce Law: Common Mistakes in Dividing Assets.

David Rice spoke on Protecting Your Business Network From Today's Full Attack Continuum at the Information Technology Managers Association TechCon 2016.

Nick Lynch presented on Fraud Trends in the Financial Services Industry at the KyCPA Forensic Accounting Conference, and he conducted fraud risk training for a financial institution's internal audit team.

Elizabeth Woodward, **Chris Anderson**, **John Herring**, **Missy DeArk**, **David Angelucci**, **Matt Smith**, and **Nick Lynch** presented on Damages, Business Valuation Concepts for Attorneys, and Forensic Accounting and Fraud in three University of Kentucky Office of Continuing Legal Education video programs.

Missy DeArk was elected to be President of the Kentucky Collaborative Family Network.