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Top Ten Tips for Tax Planning in the Recession

Tip 1: It's not too late to cut your 2008 tax bill.

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With 2008 being one of the most challenging economic periods in history, business owners and management groups are hoping for a better environment in 2009.

Unfortunately, based on most economists' predictions, businesses will likely see further contraction during the first half of the year, and any economic recovery in 2009 may be relatively minor.

As a result, businesses will need to be positioned to maximize their operating flexibility, while maximizing their after-tax earnings (or minimizing their after-tax losses).

In evaluating the optimal tax positions, taxpayers must carefully factor in the impact of any tax elections or accounting methods on their U.S. GAAP (Generally Accepted Accounting Principles) to ensure that the financial statement impact does not negatively impact the businesses credit rating and borrowing options.

In order to be well-positioned for 2009, areas of focus from a tax perspective should include:

1. **Minimizing 2008 Tax Burden**

Even though 2008 is in the history books, there are still numerous ways to reduce business taxable income after year-end.

For accrual-basis businesses, write-down of "sub-normal" goods, inventory shrinkage and other adjustments can result in significant tax benefits. Specific write-off (versus reserves) of partially or fully worthless bad debts can also generate material tax advantages. Section 179 expensing, bonus depreciation and cost-segregation analyses can further reduce 2008 taxable income. Fully accruing all year-end payables is also critical to avoid overpaying 2008 taxes.

Cash-basis taxpayers should fully analyze all prepaid expenses and credit-card charges incurred by year-end for potential tax deductibility. Depreciation and expensing of assets in excess of 2008 cash outlays, qualified retirement amounts funded after year-end, as well as any potential write-downs of assets occurring in 2008, can also generate tax deductions for last year.

2. Evaluating Prior Year Refund Potential

If the taxpayer generates a tax loss for 2008 and paid taxes in the prior two years (three years in the case of a capital loss carryback), a C Corporation can generate relatively quick cash via filing either IRS Form 4466 (Corporation Application for Quick Refund of Overpayment of Estimated Tax) or IRS Form 1139 (Corporation Application for Tentative Refund) to expedite their refunds. State refunds may also be available in certain states. Also see item 10. Below.

3. Analyze Tax Accounting Methods

In order to minimize both 2008 and 2009 taxable income, businesses should evaluate their tax elections and accounting methods to ensure that their revenue is deferred and expenses accelerated as much as possible. *For example:* Revenue recognition (goods vs. services), Expense reporting, Section 179/ Bonus Depreciation, Cost Segregation studies, Inventory methods, etc. Over the past few years, the IRS has liberalized “automatic” changes in accounting methods and generally allow up to a four-year spread on “positive” IRC Section 481 adjustments (increasing taxable income) and “negative” 481 adjustments (reducing taxable income).

4. Review Legal Structure of Operations

With valuations generally down across the board, this could be an excellent time to convert C-Corporations to S-Corporations with lower Built-In-Gain tax impact. Additionally, the use of pass-through entities can maximize the tax benefits of loss-generating businesses. This is also a good time to review any sole proprietor businesses and consider setting up appropriate entities to allow for maximum asset protection. In addition, consider setting up an Interest Charge (IC) DISC for entities with significant foreign sales income as this can result in deferral for C Corp and permanent tax savings of 10 percent or more for flow-through owners. The business will receive a deduction for commissions paid to the IC-DISC, and income distributed from the IC-DISC to its shareholders will be taxed at dividend rates.

5. Analyze Employee Benefit Structuring

Review current employee benefits structures for tax advantaged enhancements, such as: cafeteria plans, HSAs (*Health Savings Accounts*), 401(k) and qualified profit-sharing plans. Review the administrative costs of these plans as well as costs of the benefits themselves. Are these being administered as efficiently as possible, and providing maximum tax benefits for both employer and employee? Are your employees making use of all the benefits provided, or would other choices serve them better at a reduced cost to the company? Periodic information sessions with employees to cover the mechanics of these programs can ensure that both the company and the employees are obtaining optimal value.

6. Evaluate Payroll-Processing Options

Is payroll outsourced or processed internally? Does the method and provider you are using still make sense for your company? Are you paying for services you don't need? This is generally a very competitive industry, and the larger payroll companies can be very competitive on “bundled” pricing of integrated services such as: 401(k) administration; employee benefits; Workers Compensation administration and Human Resources services.

7. Analyze Earnings and Profits, AAA, etc.

With the preferential dividend/capital gain rates set to expire in 2010, and potentially under scrutiny before that time by the new administration, this is an excellent time to analyze Earnings and Profits (E&P) and AAA Accounts for potential dividend distributions. In some cases these distributions can even be made tax-free, so consider taking this opportunity to clear out prior E&P and avoid potentially higher taxes in the future.

8. Business Owners' Estate Planning

Interest rates and asset valuations are generally low right now, so this could be the ideal time to consider asset transfers for estate planning purposes. Use this opportunity to set up various estate planning entities and transfer shares in closely held business or other assets while the values are at a low point.

9. Occupancy Costs

The economic slowdown has affected property owners and managers. Commercial lease rates and overall commercial real estate values have decreased in many regions throughout the U.S. If you are considering a move to a new property, this may be the time to do so at a bargain rate. Landlords want to hang on to existing tenants, so it may also be possible to renegotiate your existing leases, or secure landlord-financed tenant improvements.

10. SALT Issues

Review current SALT (State and Local Tax Services) issues. Is sales tax being properly charged and documented? Are there any potential Use Tax issues for out of state purchases? Are you claiming all sales/use tax exemptions and credits?

Have you reviewed your property tax asset listing for valuation and dormant assets? Are you properly classifying real and tangible assets, which often have dramatically different property tax rates and depreciation schedules?

Review multi-state taxation and NEXUS (the amount and degree of business activity that must be present before a state can tax an entity's income) to make sure you are filing in all appropriate states, and that apportionment is correctly calculated. Are you taking advantage of all available income tax credits in each state, including various location based incentives (there are over 8,000 regions that offer state and federal tax incentives)?

2009 offers many uncertainties and opportunities. Therefore, the CPA, business owner or Tax Director who plans ahead will have significant advantages over their competition.

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