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Four Rules For Building A Successful Business

It's no secret that a successful business is the result of blending good business ideas with quality management. Good business ideas require imagination and creativity. Quality management means strict adherence to four rules that are essential to the success of any business.

Rule #1: Hire the right people and keep them

Any successful business knows how important it is to build an employee team. Hiring the right people is critical and motivating them to assure maximum performance and minimum turnover is just as important.

The key to motivation is compensation. The right blend of salary, performance bonuses, deferred compensation, and in some cases, equity in the business is the best way to develop a loyal and stable employee team.

It's not unusual for creative and entry level personnel to change jobs frequently. Middle management, finance, and production employees are less likely to job hop. High turnover in this group can indicate that compensation is not adequate, that hiring practices are faulty, that job conditions are frustrating, or that employees aren't given adequate resources to get the job done.

Rule #2: Maximize cash flow

Even a profitable business can find itself in serious trouble if cash flow isn't maintained. Prompt billing, careful control of receivables, and good collection practices are the answers to a healthy cash flow.

Other basic strategies to maximize cash flow include cash accumulation for a seasonal business to carry it through the slow season and use of surplus cash for low risk invest-

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Tax Points

- **Living trust may be an estate tax trap.** These trusts are often used to avoid assets from going through probate. However, trust assets can be taxed and the IRS has three years to audit an estate return. The trustee for the deceased can be held personally liable for tax liabilities owed if an IRS audit is completed after the trust distributes its assets. Should the beneficiaries not return assets then the trustee might have to pay the tax from their own funds.

- **Part-time businesses** should have their own bank accounts and bookkeeping

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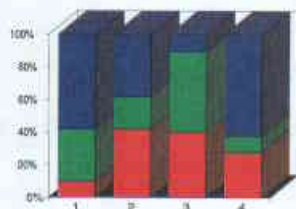
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TAX POINTS

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records. The better your records the less chance you have that the IRS will disallow your business deductions.

- **Big time tax loophole.** When you die you do not need any records to support any appreciation in your assets. The assets for tax purposes are "stepped up" to market value on the date of your death or the alternate valuation date, usually six months later.
- **Loophole: Obtain an interest free loan from the IRS** by paying to little in estimated tax payments during the year and then making up the difference by having more withheld from your paycheck at the end of the year. The IRS treats withheld taxes as being taken out evenly throughout the year.
- **Loophole: The cost for job hunting expenses** in your field is tax deductible, regardless if you succeed or not. To be deductible the job hunting expenses are included with miscellaneous itemized deductions, and are allowed to the extent their total exceeds 2% of your Adjusted Gross Income. Job hunting expenses include payments for recruiters, resumes, consultants, out-of-town travel, travel back and forth to the interviews, professional fees paid for employment contracts.



JOINT vs. SOLE OWNERSHIP: WHICH IS BETTER FOR YOU?

Joint ownership of property by spouses has certain advantages, but in some situations, it may not be as attractive as it appears. In most instances, joint ownership automatically transfers the property to the surviving spouse. This avoids probate and lowers administrative expenses. However, although joint ownership can save taxes on the estate of the first joint tenant who dies, it can result in unnecessary taxes on the estate of the surviving joint tenant.

For example, consider a situation where the husband and wife jointly own property with a value of \$3,000,000. If the husband dies, the property is automatically transferred to the wife. No estate taxes are due because the unlimited marital deduction offsets the

husband's 50% ownership of the property. However, when the surviving wife dies and leaves her \$3,000,000 estate to her children, \$1,000,000 will be subject to taxes because the applicable tax credit only offsets \$2,000,000 of the value of the estate.

The taxes on the wife's estate could be avoided if some of the property is owned individually. For example, if the husband is the sole owner of \$1,000,000 of property and the couple are joint owners of \$2,000,000 of property, all estate taxes can be avoided. When the husband dies, his \$1,000,000 can be willed directly to his children tax-free because of the applicable credit which also allows the wife's \$2,000,000 estate to be transferred to the children tax-free.

MARKETING REPORTS THAT BOOST PROFITS

Here are four key reports that can go a long way toward helping a company maximize its profits. In combination, these marketing monitors indicate where a business should direct its marketing resources to produce the best results.

- **Profitability by account.** This report lists individual accounts and shows purchases, selling prices, gross margins and allocated selling expenses. **Purpose:** weed out unprofitable accounts or take action to improve account profitability.
- **Profitability report by sales representative.** This report tracks the profitability of each salesperson's

individual accounts. **Purpose:** point out the best customers for concentrated sales efforts.

- **Profitability report by product.** This report compares the profitability of various products and their variations such as size, design, color, etc. **Purpose:** identify products for elimination or for product line expansion.
- **Profitability by market.** This report compares sales and profits within a company's sales territories. **Purpose:** monitor regional trends and identify areas that deserve an increased marketing effort.

TAX PLANNING

COMBINED PAYROLLS CAN PRODUCE TAX SAVINGS

It's not unusual for closely-held corporations to operate through more than one division and for key employees to be on the payroll of both. If an employee's combined salary from each corporation totals more than \$97,500 excess Social Security taxes might be incurred.

There's a way, however, to avoid this problem. Instead of each corporation issuing its own payroll check, designate one company in the group as a common paymaster, which can issue one check to the employee on behalf of all the compa-

nies involved. To do this, you must meet *one* of these three criteria:

- The corporations involved must have at least 50% common ownership.
- Half of the officers of one corporation must also be officers of another.
- The corporations must share at least 30% of their employees.

The result? Let's say an employee is drawing a \$60,000 annual salary from each of two corporations. Since the maximum Social Security tax is owed on

the first \$97,500 paid by each employer, the company will have to pay taxes on \$120,000 in total. If a single check from the common paymaster company is issued, \$22,500 of the total amount will be exempt from excess Social Security taxes.



GETTING THE MOST OUT OF ZERO-COUPON BONDS

Zero-coupon bonds ("zeros") can be an excellent investment but despite their widespread availability, many investors still don't understand them.

How zeros work. A zero-coupon bond is sold at a fraction of its face value. The bond pays no cash interest during its term. The *undistributed* interest from a zero is automatically reinvested every year at the same guaranteed rate. When a zero matures, all interest earned plus the principal is paid in a lump sum.

Benefits. The positive aspect of zeros is the effect of compound interest. For example, if you paid \$10,000 for a 10% ten-year zero, it would be worth about \$26,000 at maturity. But if you invested \$10,000 in a conventional bond that paid 10% a year, the interest you'd receive over ten years would total \$10,000.

Drawbacks. Even though you receive no annual interest from a zero, you must pay taxes on the bond's imputed interest each year. You can, however, avoid this tax by buying zeros through a tax-exempt IRA or Keogh account. Another caution: the market value of a zero-coupon bond can fluctuate during the period before it matures. If interest rates go up, the market value of a zero will go down. Furthermore, many zero-coupon bonds are not as liquid as other investments so it's best to hold a zero until it matures.

Zero-coupon bonds are issued by corporations, banks, and by federal and local governments. There are also mutual funds which invest only in zeros. The best strategy for buying zero-coupon bonds is to buy them through a tax exempt retirement plan and to hold them until maturity.

Savings Bonds: A Tax Shelter for You and Your Children

U.S. savings bonds are an attractive investment. They are 100% safe and sometimes pay a higher rate than longer term Treasury bonds. In addition, the tax on the interest they earn can be deferred until you cash in the bonds at which time you may be in a lower tax bracket.

The opposite may be true for your child's U.S. savings bonds. When your children cash in the bonds, they'll probably be in a higher tax bracket than they are in now. However, a child can elect *not* to defer the tax on the interest. When the interest is reported each year, it can be sheltered by a child's \$850 exclusion.