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THE VOS VOICE

"BECAUSE ACCOUNTING MATTERS AND WE KNOW IT"

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CLOSE-UP ON FINANCIAL STATEMENTS

There are three types of financial statements under U.S. Generally Accepted Accounting Principles (GAAP). Each one reveals different, but equally important, information about your company's financial performance. And, together, they can be analyzed to help owners, management, lenders and investors make informed business decisions.

Profit or loss

The income statement shows revenue and expenses over the accounting period. A commonly used term when discussing income statements is "net income," which is the income remaining after all expenses (including taxes) have been paid.

It's also important to check out the company's "gross profit." This is the income earned after subtracting the cost of goods sold from revenue. Cost of goods sold includes the cost of direct labor and materials, as well as any manufacturing overhead costs required to make a product.

The income statement also lists sales, general and administrative (SG&A) expenses. They reflect functions, such as marketing and payroll, which support a company's production of products or services. Often, SG&A costs are relatively fixed, no matter how well your business is doing. Compute the ratio of SG&A costs to revenue. If the percentage increases over time, business may be slowing down.

Financial position

The balance sheet tallies your company's assets, liabilities and net worth to create a snapshot of its financial health on the financial statement date. Assets are customarily listed in order of liquidity. Current assets (such as accounts receivable) are expected to be converted into cash within a year, while long-term assets (such as plant and equipment) will be used to generate revenue beyond the next 12 months.

Similarly, liabilities are listed in order of maturity. Current liabilities (such as accounts payable) come due within a year, while long-term liabilities are payment obligations that extend beyond the current year.

Because the balance sheet must balance, assets must equal liabilities plus net worth. So, net worth is the extent to which assets exceed liabilities. It may signal financial distress if your net worth is negative. Other red flags include:

- Current assets that grow faster than sales, and
- A deteriorating ratio of current assets to current liabilities.

These trends could indicate that management is managing working capital less efficiently than in prior periods.

Cash inflows and outflows

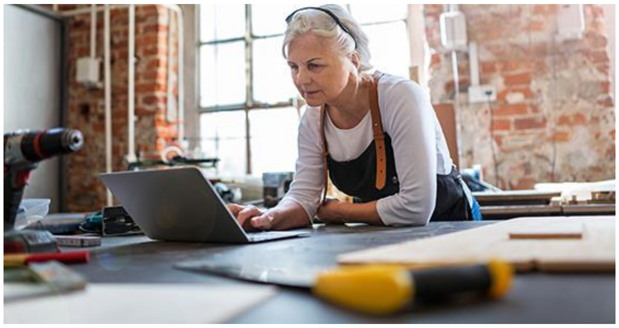
The statement of cash flows shows all the cash flowing in and out of your company during the accounting period. For example, your company may have cash inflows from selling products, borrowing, and selling stock. Outflows may result from paying expenses, investing in capital equipment and repaying debt.

The statement of cash flows is organized into three sections: cash flows from operating, financing and investing activities. Ideally, a company will generate enough cash from operations to cover its expenses. If not, it may need to borrow money or sell stock to survive.

Ratios and trends

The most successful businesses continually monitor ratios and trends revealed in their financial statements. Contact us if you need help interpreting your financial results.

"Because Accounting Matters"



BUY VS. LEASE: BUSINESS EQUIPMENT EDITION

Life presents us with many choices: paper or plastic, chocolate or vanilla, regular or decaf. For businesses, a common conundrum is buy or lease. You've probably faced this decision when considering office space or a location for your company's production facilities. But the buy vs. lease quandary also comes into play with equipment.

Pride of ownership

Some business owners approach buying equipment like purchasing a car: "It's mine; I'm committed to it and I'm going to do everything I can to familiarize myself with this asset and keep it in tip-top shape." Yes, pride of ownership is still a thing.

If this is your philosophy, work to pass along that pride to employees. When you get staff members to buy in to the idea that this is your equipment and the success of the company depends on using and maintaining each asset properly, the business can obtain a great deal of long-term value from assets that are bought and paid for.

Of course, no "buy vs. lease" discussion is complete without mentioning taxes. The Tax Cuts and Jobs Act dramatically enhanced Section 179 expensing and first-year bonus depreciation for asset purchases. In fact, many businesses may be able to write off the full cost of most equipment in the year it's purchased. On the downside, you'll take a cash flow hit when buying an asset, and the tax benefits may be mitigated somewhat if you finance.

Fine things about flexibility

Many businesses lease their equipment for one simple reason: flexibility. From a cash flow perspective, you're not laying down a major purchase amount or even a substantial down payment in most cases. And you're not committed to an asset for an indefinite period — if you don't like it, at least there's an end date in sight.

Leasing also may be the better option if your company uses technologically advanced equipment that will get outdated relatively quickly. Think about the future of your business, too. If you're planning to explore an expansion, merger or business transformation, you may be better off leasing equipment so you'll have the flexibility to adapt it to your changing circumstances.

Last, leasing does have some tax breaks. Lease payments generally are tax deductible as "ordinary and necessary" business expenses, though annual deduction limits may apply.

Pros and cons

On a parting note, if you do lease assets this year and your company follows Generally Accepted Accounting Principles (GAAP), new accounting rules for leases take effect in 2020 for calendar-year private companies. Contact us for further information, as well as for any assistance you might need in weighing the pros and cons of buying vs. leasing business equipment.

> *"The Best Preparation for Tomorrow is Doing Your Best Today."*
>
> *-- H. Jackson Brown, Jr.*

SELLING YOUR HOME? CONSIDER THESE TAX IMPLICATIONS

Spring and summer are the optimum seasons for selling a home. Moreover, interest rates are currently attractive, so buyers may be out in full force in your area. Freddie Mac reports that the average 30-year fixed mortgage rate was 4.14% during the week of May 2, 2019, while the 15-year mortgage rate was 3.6%. This is down 0.41 and 0.43%, respectively, from a year earlier.

Nevertheless, before you contact a realtor to sell your home, you should review the tax considerations.

Sellers can exclude some gain

If you are selling your *principal* residence, and you meet certain requirements, you can exclude up to $250,000 ($500,000 for joint filers) of gain. Gain that qualifies for the exclusion is also excluded from the 3.8% net investment income tax.

To qualify for the exclusion, you must meet these tests:

- **The ownership test.** You must have owned the property for at least two years during the five-year period ending on the sale date.

Please see *Selling Your Home? Consider These Tax Implications* on page 3

Selling Your Home? Consider These Tax Implications **from page 2**

- **The use test.** You must have used the property as a principal residence for at least two years during the same five-year period. (Periods of ownership and use do not need to overlap.)

In addition, you cannot use the exclusion more than once every two years.

Handling bigger gains

What if you are fortunate enough to have more than $250,000/$500,000 of profit when selling your home? Any gain that does not qualify for the exclusion generally will be taxed at your long-term capital gains rate, provided you owned the home for at least a year. If you did not, the gain will be considered short term and subject to your ordinary-income rate, which could be more than double your long-term rate.

Other tax issues

Here are some additional tax considerations when selling a home:

Keep track of your basis. To support an accurate tax basis, be sure to maintain thorough records, including information on your original cost and subsequent improvements, reduced by any casualty losses and depreciation claimed based on business use.

Be aware that you cannot deduct a loss. If you sell your principal residence at a loss, it generally is not deductible. However, if part of your home is rented out or used exclusively for your business, the loss attributable to that portion may be deductible.

If you are selling a *second* home (for example, a vacation home), be aware that it will not be eligible for the gain exclusion. However, if it qualifies as a rental property, it can be considered a business asset, and you may be able to defer tax on any gains through an installment sale or a Section 1031 exchange. Alternatively, you may be able to deduct a loss.

Your home is probably your largest investment. So before selling it, make sure you understand the tax implications. We can help you plan ahead to minimize taxes and answer any questions you have about your situation.

"You Don't Have to See the Whole Staircase, Just Take the First Step."

--Martin Luther King

IRS CORNER

IRS Highlights Credits and Deductions for Businesses During Small Business Week

IR-2019-93; WASHINGTON — During Small Business Week, the Internal Revenue Service reminds small business owners and self-employed individuals to take deductions and credits that will help their bottom line.

Reviewing options and eligibility now can help business owners better estimate their tax situation and plan ahead. Here are just a few key deductions and credits that can benefit small business taxpayers.

Deductions

Qualified business income deduction

Many individuals, including owners of businesses operated through sole proprietorships, partnerships, S corporations, trusts and estates may be eligible for a qualified business income deduction, also called the section 199A deduction. Some trusts and estates may also claim the deduction directly.

The deduction allows them to deduct up to 20 percent of their qualified business income (QBI), plus 20 percent of qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income. Income earned by a C corporation or by providing services as an employee isn't eligible for the deduction.

The deduction is available for tax years beginning after Dec. 31, 2017. Eligible taxpayers can claim it for the first time on their 2018 federal income tax returns filed in 2019.

Business losses

The TCJA also made changes to losses. Under TCJA, losses from a trade or business are now limited to $250,000 or $500,000 for a joint return. This includes activities reported on Schedule C by a self-employed individual and farming activities reported on Schedule F. It also includes being an employee and certain activities reported on Schedule E. Excess business losses that are no longer allowed are treated as a net operating loss (NOL) and carried forward to the following tax year.

For most taxpayers, NOLs arising after 2017 can only be carried forward. However, certain farming businesses and insurance companies – other than life insurance – can still use a two-year carryback for certain losses. After Dec. 31, 2017, the net operating loss deduction is limited to 80 percent of taxable income. Rules for existing or pre-2018 NOLs remain the same.

Business expenses

Business expenses are usually deductible if the business

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operates to make a profit. To be deductible, a business expense must be both ordinary and necessary. An ordinary expense is one that is common and accepted in the trade or business. A necessary expense is one that is helpful and appropriate for the trade or business. An expense does not have to be indispensable to be considered necessary. Business expenses include:

- **Business use of a home** – If a taxpayer uses part of their home for business, part of their home expenses may be deductible. These expenses may include mortgage interest, insurance, utilities, repairs and depreciation. Alternatively, a simplified method is available for figuring this deduction. Special rules and limits apply. See Publication 587 for details.
- **Business use of a car** – If a taxpayer uses their car in their business, they can deduct car expenses. If they use it for both business and personal purposes, they must divide expenses based on actual mileage. For details, including special recordkeeping rules, see Publication 463.
- **Meals and entertainment** – In general, taxpayers can deduct 50 percent of the cost of business meals if the taxpayer -- or an employee of the taxpayer -- is present and the food or beverages are not lavish or extravagant.
- **Rent expense** – In general, a taxpayer can deduct rent as an expense only if the rent is for property used in their trade or business. If they have or will receive equity in or title to the property, the rent is not deductible.
- **Interest** – Business interest expense is an amount charged for the use of money a taxpayer borrowed for business activities. Limits and special rules may apply. See basic questions and answers about the limitation on the deduction for business interest expense for more information.
- **Taxes** – A taxpayer can deduct various federal, state, local, and foreign taxes directly attributable to their trade or business as business expenses.

Publication 535, Business Expenses, has more information about these and other deductible business expenses, including employee related expenses such as employees' pay, retirement plans and insurance.

Credits

General business credits

The general business credit includes about two dozen tax credits for a variety of businesses and business activities. Often, a taxpayer who qualifies for one or more of these credits but is unable to use them for a given tax year can carry them back to a prior year or forward to future years. See Form 3800 and its instructions for details.

Employer credit for paid family and medical leave

TCJA added this new general business credit that qualified employers may claim based on wages paid to qualifying employees on family and medical leave. To claim the credit, eligible employers must have a written policy in place that meets certain requirements, including providing at least 2 weeks of paid leave to full-time employees (prorated for employees who work part time) and the paid leave must be at least 50 percent of the wages normally paid to the employee. For TY 2018, the employee's prior year compensation from the employer must have been $72,000 or less. See Notice 2018-71 and instructions for Form 8994 for details.

Tax credits can help employers hiring new workers

With many businesses now facing a tight job market, there is another general business credit that may help. The long-standing Work Opportunity Tax Credit (WOTC) is designed to help employers who hire long-term unemployment recipients, certain veterans, recipients of certain kinds of public assistance and other categories of workers with employment barriers. Certification requirements and other special rules apply. To find out more, visit IRS.gov/wotc.

Find more information about business tax credits on IRS.gov.

"The Secret of Getting Ahead is Getting Started."

--Mark Twain

WHERE'S MY REFUND?

Are you wondering where your tax refund is? According to the IRS, most refunds are issued in less than 21 calendar days. If you are curious about when yours will arrive, you can use the IRS "Where's My Refund?" tool. Go to https://bit.ly/2cl5MZo and click "Check My Refund Status." In some cases, taxpayers may be notified that all or part of their refunds are not going to be paid because they're going to "offset" past-due debts. These include federal or state tax obligations; past-due child and spousal support; and certain delinquent student loans. If you have questions about your refund, contact us.