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# THE PLANNER

THE NEWSLETTER FOR THE AICPA PERSONAL FINANCIAL PLANNING DIVISION

## 1989 Tax Planning Ideas

**by David E. Karr, CPA, JD. Senior Tax Manager, Grant Thornton, McLean, Virginia and member of the PFP Practice Subcommittee**

With the end of the year fast approaching, the time has come to consider your clients' year-end tax planning. Throughout this process, it is important to realize that you and your clients will be planning for more than just this year: You will be planning for next year and dealing with the consequences of your planning from last year. Throughout the tax planning process, remember that reducing a client's tax liability should be considered only in light of the overall economics of any transaction. If the economics of a transaction dictate that action should be taken, then it is the time to do so—regardless of the tax rates in effect.

Since the Tax Reform Act of 1986, year-end tax planning has changed significantly. When the highest marginal tax bracket was 50% in 1986, the goal was to defer income into 1987 when the maximum tax rate was 38.5%. The same was true for deferring income from 1987 into 1988—to take advantage of the maximum 28% tax rate and 33% marginal tax rate.

In 1988, the conventional wisdom was that tax rates would rise. This thinking was due in part to the budgetary and deficit problems facing the country. In anticipation of a tax rate increase, some tax advisers recommended that their clients accelerate their income into 1988 in order to take advantage of the comparatively lower tax rate.

With these thoughts in mind, the following abbreviated list offers 1989 tax planning ideas for your clients to consider prior to the end of the year:

1. Depending on the status of legislation to increase individual income tax rates at the time the planning takes place, it may be beneficial for clients to accelerate their income into 1989. The Senate Finance Committee voted recently to increase the highest individual tax rate from 28% to 33%. While this has not become law as of this date, it is an indication of things to come.
2. To increase your client's taxable income, consider the deferral of payment of tax-deductible expenses from 1989 to 1990. Moreover, with respect to the higher limitation on certain miscellaneous itemized deductions, it may be to the client's advantage to group these expenses/deductions (into either year) in order to maximize their tax benefits.
3. Consideration should be given to the generation of passive activity income. For example, if your client has a passive activity—such as a rental property, which can be sold to maximize

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### DIVISION NEWS ALERT

**Division's National PFP Conference**—January 8 and 9, 1990, PGA Sheraton Resort in Palm Beach Gardens, (15 minutes from West Palm Beach) Florida (see article on page 4)

**State Society PFP Committee**—Chairperson's Roundtable—January 10, 1990, PGA Sheraton Resort in Palm Beach Gardens

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a gain—you might suggest a year-end sale.

This may enable the client to offset the gain of the sale against any current year or suspended losses that might otherwise be unusable under the passive activity limitations. Long-term strategies to deal with passive losses should also be investigated.

4. Capital gains for this year will be taxed at the same rate as other income. Due to the phase-out of the 15% tax bracket and personal exemptions, it is possible that an individual's marginal rate could be as high as 33%, thereby subjecting your client's capital gains to this same rate.

   The President and the House have proposed to lower the long-term capital-gains rate on certain stock transactions. With this proposal in mind, it may make sense to defer the timing of any such gains until 1990, assuming that the underlying economics justify this decision.

5. Long-term capital losses could be offset against other capital gains without reduction. As a result, your client may want to consider bond swaps to reduce their 1989 tax. Under the wash sale rule, losses cannot be deducted from the sale of securities if, within 30 days either before or after the sale of securities, the same or substantially identical securities are acquired. Because of this rule, bond swaps may be preferable to equity swaps. You are more likely to find a bond—rather than a stock—having similar characteristics to the one you are now holding without falling into the "same or substantially identical" trap.

6. The interest expense deduction has become more restrictive: therefore, the use of home equity loans to finance consumer purchases may be more desirable for your client. Counsel clients to exercise caution, though, as home equity loans involve risks that may not be appropriate for many taxpayers because of the temptation of easy access to their equity.

7. If your client has tax shelter investments or has entered into other transactions that are likely to generate significant tax preference items, you may need to examine their tax situation to determine if they are subject to the alternative minimum tax (AMT). In this regard, you might want to consider:
   - Controlling the timing of certain items that raise the AMT.
   - Reducing or eliminating other tax preference items by electing to capitalize certain items eligible for special amortization or by changing depreciation methods on certain property.
   - Deferring deductions. If a client is not subject to the AMT in 1990, the deferred deductions will create a 28% (or higher) benefit instead of a 21% benefit (the AMT rate) in 1989.

8. Review your client's retirement plan options to determine if they can open or contribute to a Keogh, SEP, IRA, 401(k) or 403(b) plan.

9. See if your client can take advantage of the $10,000 annual gift tax exclusion. Also, this is the last year to act on the estate tax freeze provision, as well as the Gallo amendment that addresses the generation-skipping tax. A complete estate plan developed by the CPA can help determine if the client qualifies.

10. In order to avoid any tax penalty, review your client's payroll tax withholding to determine if the lesser of 90% of this year's estimated federal tax liability or 100% of last year's tax liability will be paid by year-end.

Year-end tax planning for your clients should be an ongoing process. During the last few months of the year, fine tune your clients' planning as their income and expenses become more definite. It can also be a chance to develop long-range financial plans. If you have not yet begun this process, there is still time for optimum planning. The ideas presented here are a good starting point.

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## Creating a Profitable PFP Practice from Tax Season

Larry Fowler, CPA/APFS, had a goal of building a successful financial planning practice when he joined his current firm, Searing, Gitelson & Keeslar, two and a half years ago. He chose tax season to begin the process.

During that first tax season, the firm sent out two documents along with its standard tax organizer. The first document was a client profile or summary balance sheet. The second was a questionnaire asking the client questions such as: "Do you plan to pay for your children's college education?" "Are you fully funded in your company's 401(k)?" "Do you have a will?" When clients came in to discuss their taxes, they were requested, if appropriate, to give additional information.

During the tax interview, clients were asked whether they wanted the firm's assistance in addressing planning issues that came to the forefront. If there was an immediate need, the firm made arrangements to pursue a planning engagement; otherwise, planning was deferred until summer.

When completing the returns, the firm's tax preparers were asked to be on the alert for planning issues, to note pertinent information and to record that information along with the client's social security number on a short, half-page client contact form. The data was then input into a centralized database for later access.

From the information gathered during that tax season, the firm sent out 100 letters (out of approximately 700 tax clients). Out of that group, there were 24 responses and ultimately 12 of them became financial planning clients.

The first year was so successful that Larry continued the internal marketing program during the second tax season: "We send letters to clients following up on data gathered during tax season. These letters are sent out in about August."

Clients did not object to the solicitation for additional information, and were responsive and pleased at the firm's interest in them. Some clients even indicated they were hoping for this type of service but were unsure of where to go for it.

### Ongoing Services

Larry uses a similar tax season system to update the client's plan. Each year, when the financial data is gathered during tax time, there is an annual review. If immediate action needs to be taken, the firm handles it. If not, the plan is revised after tax season. This system helps the client gather the necessary materials for tax time anyway.

**Larry is a member of the PFP Executive Committee and Practice Subcommittee.**

### Partner Involvement

Larry explains that cooperation and support from the firm's partners are keys to a successful PFP practice. His previous experience with another firm did not offer this kind of support: as a result, the PFP practice floundered.

In Larry's present situation, the firm's partners promote financial planning services to their auditing and accounting clients. As a result of these efforts, the firm has significantly increased its financial planning business.

The partner-in-charge of quality control has also been instrumental in the PFP practice. Larry explains that he was very helpful in setting up the systems and workpaper procedures for financial planning—efforts that helped keep the financial planning engagements focused.

### Future Plans

Currently, about 10% of the firm's fees come from PFP engagements. The practice has been growing steadily, relying strictly on soliciting the firm's existing clients.

The firm will be co-sponsoring its first seminar with a local bank and a law firm to attract additional clients. Larry foresees this as the first step toward expanding the PFP practice beyond current clients.

## PFP Division's Technical Conference

On January 8–9, 1990, the PFP Division is sponsoring its third annual technical conference at the PGA Sheraton Resort in Palm Beach Gardens, Florida. The theme of this year's conference is "PFP in the 1990s." The conference is designed to provide practitioners with the latest personal financial planning tools and techniques that will enable them to meet their clients' needs in the 1990s. The conference offers 26 concurrent sessions and 3 plenary sessions over a two-day period.

### Concurrent Sessions

Participants may elect to follow the asset allocation track, which consists of four sessions covering asset allocation and the use of fixed income, international investments, equities and real estate to achieve clients' goals.

Another track is personal financial planning for the major life phases. Using the case-study approach, participants gain hands-on experience in addressing the financial planning needs of a young doctor in the 30s, a successful closely-held business owner in the 40s and a successful corporate executive in the 50s. Although a track may be a day or two in length, participants can benefit from attending one or all related sessions.

Several of the concurrent sessions address major issues that participants and their clients will deal with as they approach the 1990s. As people live longer and become more skeptical of the Government's ability to provide for their retirement needs, retirement planning and long-term care become important issues. PFP for Graying America deals with new strategies for retirement planning. Another session, Financing Long-Term Care, addresses funding long-term care through public and private insurance programs and discusses how to select and integrate long-term care into the financial plan.

Several concurrent sessions are designed to provide new financial planning strategies: PFP for High Income Executives focuses on planning opportunities and techniques for wealthy corporate executives. How Clients' Goals Can Be Achieved With New Insurance Products covers how to use survivorship life insurance to minimize gift and estate taxes on life insurance proceeds.

Although most of the sessions are at the advanced level, four sessions have been designed for those who want to learn the fundamentals of PFP: Managing a Profitable PFP Practice, Marketing a PFP Practice, Developing the PFP Process and Tips-PFP Ideas. Again, participants can attend any or all sessions.

### Plenary Sessions

Three plenary sessions that will have broad appeal are PFP for the Divorcing and the Divorced Client, PFP in the 1990s and Coping With Change and Stress. PFP for the Divorcing and the Divorced Client covers the issues involved in a divorce, the role of the financial planner and how to develop competence in domestic relations issues.

Everyone wants to know what the future holds, and financial planners are no exception. In PFP in the 1990s, John Freeman Blake, Esq., Stanley H. Breitbard, CPA, and Larry Fowler, CPA/APFS—practitioners of different disciplines and with firms of different sizes—will share their views on the future of personal financial planning.

Changes and uncertainty about the future can create stress. Stress can interfere with clients' ability to make financial decisions. In Coping with Changes and Stress, practitioners will learn how to help their clients make financial decisions during times when they are under pressure and how to deal more effectively with their own problems.

In addition to these sessions, there will be three interesting luncheon speakers:

**January 8**—Michael Lipper, Chief Executive Officer of Lipper Analytical Services. *Topic:* Mutual funds in the 1990s.

**January 9**—Michael Azorsky, Chairman of the PFP Executive Committee. *Topic:* Activities of the PFP Division.

**January 9**—Herbert L. Finkston, Director of the AICPA Professional Ethics Division. *Topic:* Implementing the FTC agreement with respect to commissions and contingent fees.

"PFP in the 1990s" will offer participants an opportunity to learn more about the latest personal financial planning tools and techniques, as well as earn up to sixteen (16) CPE credits. It also provides a forum where practitioners can meet and exchange ideas. For further information on the conference, call (212) 575-3644 and request a conference brochure, which also describes the recreational and sightseeing opportunities available at the PGA Resort Sheraton in Palm Beach Gardens.

## Executive Compensation Packages
## First of a Series

### Section 162 Executive Bonus Plan

Companies are constantly looking for approaches to attracting and keeping key employees in today's competitive marketplace. One of the ways in which organizations can accomplish this is through the use of new and innovative compensation packages tailored to fit employee needs and designed to provide adequate financial protection.

One type of compensation technique designed to take maximum advantage of these changes is the Executive Bonus Plan, or the executive bonus life insurance plan. Instead of rewarding an executive with straight cash, the employer uses the bonuses of selected key employees to pay for premiums on a life insurance policy. Thus, the Executive Bonus Plan provides selected key people with life insurance protection that is paid for by the employee through annual salary increases given by the employer. The employee, as insured-owner, has the right to name the policy beneficiary and has complete access to the cash build-up in the contract.

#### How the Plan Works

The employer gives the employee a bonus. The employer pays this bonus either directly to the insurance company or provides the amount necessary to fund the premiums taken out on the employee's life. In either case, the bonus represents compensation income to the employee, and is, therefore, taxable. The corporation deducts the amount of the bonus as an ordinary business expense under §162(a)1, subject to the reasonable compensation rules.

However, let's go one step further. Assume the employee needs to pay a tax on the bonus. There are two ways in which the employee gets the money to do this:

1. *Double Bonus Plan.* The employer gives the executive an additional bonus to pay the tax on the first bonus. This is done by "bonusing" the employee 139% of the insurance premium. Why 139%? Because this is the reciprocal of the executive's tax bracket (1 / 1-.28)

2. *Policy Dividends.* Since the executive owns the policy, he or she may take the dividends in the form of cash and apply them toward the premium. Dividends, however, are not guaranteed and are dependent upon a variety of factors such as investment yields, mortality experience and expense of operations.

The executive also must consider estate and gift tax aspects. The proceeds of the life insurance are included in the employee's gross estate when incidents of ownership are retained. It is excludible from the gross estate when no incidents of ownership are retained for at least three years prior to death.

If the spouse is the beneficiary, the unlimited marital deduction will apply. If the gross estate inclusion is a concern for the executive, however, the plan should be designed at its inception with third-party ownership.

**The most attractive feature of the Executive Bonus Plan may be its exemption from nondiscrimination rules and Dept. of Labor Administrative reporting rules.**

An example of this would be the spouse of an insured-employee or an irrevocable trust created by the insured-employee. If estate tax problems become a concern after the policy is implemented, the participant may "gift" the existing policy to a third-party owner.

From the employer's point of view, the most attractive feature of the Executive Bonus Plan may be its exemption from the nondiscrimination rules and Department of Labor administrative reporting rules applicable to most other types of fringe plans. Owners of a closely-held business may pick and choose the employees they wish to cover and limit the plan to owner-employees who desire substantial life insurance coverage. This also allows the owner-employees to build an asset base, tax deferred, which can be used for lifestyle costs at retirement if the business itself cannot be sold. It also can be an effective sheltering technique for unneeded cash by the owner.

(The next issue of The Planner will cover the second topic in this series: split dollar life insurance plans.)

## PFP LEGISLATIVE ACTIVITY

As several state legislatures adjourned for the year, a few are conducting studies to determine the need for regulation of financial planners. A state-by-state summary of legislative activity follows.

**Illinois**—A bill (HB-2752) amending the state securities law to expand the definition of investment adviser to include financial planners was placed on hold. The CPA state society plans to meet with the director of state securities to discuss its concerns about the proposed bill. No action is expected until the Spring of 1990.

**Indiana**—The state securities division is proposing to introduce legislation to expand the definition to include financial planners in 1990. The proposed bill would make it difficult for CPA financial planners to be excluded from the registration requirement if they call themselves financial planners.

**New Hampshire**—A six-member legislative committee was appointed to conduct a general study on the financial services industry. The committee will hold its first of several meetings on November 1. Each meeting will focus on one of the financial service sectors and representatives from these sectors will be invited to attend. A committee report is expected by December 1.

**New York**—Eight bills (AB 3445, ABN 6242, AB 8146, AB 8776, SB 3182, SB 3553/AB 5748, SB 1138 and SB 3812) proposing the regulation and registration of financial planners were introduced in 1989. The bills died when the legislature adjourned at the end of June. It is expected that new financial planning bills will be introduced in 1990.

**Utah**—The Business and Labor Interim Committee of the Utah House of Representatives will vote to introduce Draft 90-FL-0096 as an interim bill. The draft proposes to require disclosure and registration of financial planners. It will require all financial planners and those who hold out as financial planners to register and make certain disclosures. If the draft becomes an interim bill, educational requirements and testing may be added.

**West Virginia**—A bill (HB-2547) to regulate and license financial planners was introduced. It con-

### STATE REGULATION OF INVESTMENT ADVISERS AND FINANCIAL PLANNERS

| No Investment Adviser or Financial Planner Requirements | Investment Adviser Regulation | | Investment Adviser & Financial Planner Regulation: Includes term "Financial Planner" with definition of Investment Adviser (NASAA Model Amendments) | + Holding out provision as well (IAFP provision) |
|---|---|---|---|---|
| Alabama | Alaska | Missouri | Virginia | Georgia |
| Arizona | Arkansas | Montana | North Carolina | Washington |
| Colorado | California | Nebraska | North Dakota | Maryland[3] |
| D.C. | Connecticut | Nevada | South Dakota | |
| Iowa | Delaware | New Hampshire | Montana | |
| Massachusetts | Florida | New Jersey | Oklahoma | |
| Ohio | Hawaii | New Mexico | | |
| Vermont | Idaho[1] | New York | | |
| Wyoming | Illinois | Oregon | | |
| | Indiana[2] | Pennsylvania | | |
| | Kansas | Rhode Island | | |
| | Kentucky | South Carolina | | |
| | Louisiana | Tennessee | | |
| | Maine | Texas | | |
| | Michigan | Utah | | |
| | Minnesota | West Virginia | | |
| | Mississippi | Wisconsin | | |

[1]Excludes licensed CPAs and PAs from definition of investment adviser

[2]NASAA model amendments—but does not include financial planner regulation

[3]Excludes persons regulated by a state agency, board or commission with financial planners disciplinary powers from definition of investment adviser except if commissions are accepted or funds or securities held in trust.

Prepared by the AICPA State Legislation Department
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**Editor:** Sophia Modi

tained a broad definition of financial planner (see the April/May 1989 issue of The Planner). It died when the legislature adjourned. A pre-filed bill has been introduced for the 1990 session.

As another legislative year draws to an end and bills affecting CPA financial planners have passed or died, a new legislative year is on the horizon. Many state societies have reported that in 1990 their state legislatures will be either considering new bills or studying the need for regulation of financial planners. In the past year, state societies have been effective in preventing the enactment of many bills that would have been detrimental to CPAs providing financial planning services.

In the chart on page 6, a summary of state regulation of investment advisers and financial planners indicates that nine states have financial planner regulations, and the number can increase. If you are aware of possible legislation in your state or if you would like to help in opposing it, contact your state society. For additional information, call John Sharbaugh in the AICPA's State Legislation Department at 202-737-6600.

## Seminar Savvy

**By Kevin Roach, CPA, a member of the PFP Practice Subcommittee and Partner, Price Waterhouse, New York, New York**

A comprehensive practice development strategy for providing personal financial planning services includes using seminars to present your firm's expertise and capabilities to both clients and prospective clients. Seminars are not the only method of practice development, but they are an effective tool when used properly.

The primary objective of a personal financial planning seminar is to market the firm's services. As a practice development tool, seminars become a forum for reaching a large number of selected people with the message that you want to convey. Alternatively, if marketed creatively, the seminar can become an engagement rather than overhead. In either case, you can design the seminar to address a particular issue or provide an overall educational experience, and leave the attendees with the feeling that they want to come to you when they need assistance with their financial affairs. Achieving this objective requires careful planning and attention to details.

### Planning for the Seminar

Organizing the seminar should begin 60 to 90 days before the planned event. The first step is selecting the target market. In deciding on attendees, select either prospective clients or existing clients whose relationship can be expanded to include financial planning. The potential attendees should have common interests and needs that are compatible with the experience and services offered by the firm.

The size of the audience can vary according to the target market and the desired marketing objectives. Although CPAs can give seminars for groups of several hundred people, groups of 20 to 40 generally work best. If your target market is corporate CEOs, you may find that a small, intimate group is more appropriate. Some firms find that inviting 8 to 10 senior executives to a short, early morning breakfast seminar is very effective. Consider inviting spouses to seminars; they are often a vital part of the financial planning process.

The seminar topic should be timely and of particular interest to the audience. If not, the seminar will be poorly attended and the success of future seminars will be jeopardized.

After the topic is selected, the success of the seminar will depend largely on the discussion leader's skill. The leader needs excellent public speaking skills, the commitment to be properly prepared, and a thorough knowledge of the topic to be discussed. An effective leader is in tune with the audience, objective in presenting the material, and, most importantly, able to simplify the complexities of the subject for the audience.

The firm should finalize all details—the attendees, discussion leader, location, date and time—at least 45 days before the seminar. It should mail the invitations about 21 to 30 days before the seminar. Reconfirm site reservations and other arrangements weekly and confirm final arrangements the day before the seminar. Prepare handouts about three weeks ahead of time, with allowances for last minute changes. During the last week, have the speakers rehearse the program and have someone call the invitees to confirm their attendance. Attention to these details will pay big dividends.

### Conducting the Seminar

The actual presentation sets the tone of the seminar. If the presentation has rough spots or if things appear to go wrong during the presentation, the audience may subconsciously infer that the firm is not well prepared. Consequently, the audience may feel reluctant to place their trust in the firm.

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The presenter and the firm representatives should be well prepared and enthusiastic. Have greeters meet the guests as they arrive, and be available to talk with the attendees at breaks following the seminar. The firm's partners and managers who extended the invitations should certainly be in attendance.

It is often advantageous to have the attendees participate in the program rather than just be listeners. Effective methods include using small-group breakout sessions, as well as providing workbooks that allow the attendees to apply the information discussed to their own situation. Additionally, if the host firm has the capability of generating automated financial plans, it can prepare an individualized report for each attendee ahead of time for use during the seminar.

Be prepared for the unexpected. A projector bulb can fail, so have a spare or two on hand. Similarly, double check for an ample supply of markers and chalk, as well as an extra extension cord. Run through the slides at the last minute to ensure proper placement. Have name tags for easy introductions. Finally, before concluding, ask each attendee to fill out an evaluation form.

### Seminar Follow-up

Follow-up is the most important part of any seminar. Tabulating the evaluations prepared by the attendees and discussing the results will provide valuable insights for improving future seminars. The firm's bottom line is improved, however, only if the firm's representatives who extended the invitations personally call each attendee to discuss details of the seminar topic and how they apply to the individual. Regardless of how motivating the presentation, personal follow-up is an absolute requirement.

### A New Approach

Firms traditionally conduct seminars as a practice development tool to attract new clients for the firm's services. It is a two-step process requiring a significant investment of time and money. Why not get paid for the seminar as well?

Employers are continually faced with the difficult task of communicating human resource issues to employees. Since CPAs are trusted as objective, knowledgeable and credible advisers, they are now being engaged to give seminars to employees on topics such as the installation of 401(k) plans, downsizing and early retirement programs. This type of engagement may require that the seminar be given in several locations.

The fees for these seminars can be substantial. Pricing should include the time for the presentation, as well as the time for preparation and researching the client's employee benefit programs. Such engagements often include financial planning for the executives and other employees, especially if it is part of a downsizing or early retirement program.

### Summary

Whether a seminar is used as a practice development tool or to generate a fee, it is an excellent method of reaching a large number of people you would like as clients. Well planned and professionally executed seminars on relevant, timely topics are an effective tool for building your firm's bottom line and its reputation in the community.

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