GCG WEALTH MANAGEMENT, INC.

See disclaimer on final page ■ October 2016

Newsletter

Empower your Family, Wealth, Life

Properly Insuring Your Business

Transferring Your Family Business

Retirement Planning Options for Business Owners

Self-Employed Benefit Plans

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Properly Insuring Your Business

No matter how careful you are in running your business, accidents happen. And no matter how big or small your business, you'll have to plan for these and other risks if you want your business to thrive. One way to do this is with insurance.

Imagine this: Your custom-made cabinetry business is thriving. You have a handful of talented employees and a stack of orders. Then, the unthinkable happens. You or one of your employees is severely injured using the equipment. Or a fire damages all of the cabinets you've spent the last few months building. Or a customer calls to tell you that the new cabinets you installed yesterday just fell and crashed onto her kitchen floor.

Protect your business from physical destruction

Your business is situated somewhere--an office park, a warehouse, a barn. And just like your home, this structure (and all of its contents) is susceptible to damage from many causes. Property and casualty insurance provides coverage for losses due to the physical damage or destruction of your business. With the right policy, neither fire nor exploded boiler can put you out of business. Everything from your office building to your cabinets to your water cooler can be covered.

You can buy various types of insurance protection separately, or you can purchase one package that covers many potential hazards. Among the forms of coverage you can purchase are:

- Building and equipment insurance: This protects you if your facility or equipment is damaged or destroyed
- Valuable papers insurance: This protects you if the documentation supporting your accounts receivable (or other valuable business records) is lost or destroyed
- Crime insurance: This protects your business in case of theft
- Business interruption insurance: This protects you by replacing some or all of your operating cash flow if your business is unable to maintain its normal operations for a period of time due to a covered event

Keep your business afloat if you or a key employee dies or becomes disabled

If you were to die prematurely or become permanently disabled and could no longer work, would your business survive financially? It's easy to believe that such a tragedy won't befall you. Consider, however, that accidents happen not only on the job but also at home, and illness can strike anyone. Though the death or disability

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of an owner may be a minor issue for large businesses, small businesses may find themselves in a bind. And if you're a sole proprietor, you're personally responsible for all of the debts of your business, so everything you own could be repossessed if you're unable to pay your bills.

To survive a money crunch, your business can purchase life insurance and disability insurance to cover you, with the business named as the beneficiary. Upon a triggering event (death or disability), the policy will pay your business a certain amount of money, which it can use to cover its normal operating expenses like rent, utilities, employee salaries, advertising, and maintenance costs.

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Note: These types of policies are different from workers' compensation insurance, which nearly all states require businesses to have. Workers' compensation insurance provides compensation to your employees if they're injured at work or get sick from job-related causes. Once an employee opts to receive benefits under such a policy, he or she is usually prohibited from suing your business for the same injuries.

Protect your business assets if someone threatens or sues your business

If your cabinet installation goes awry and your best customer (or so you thought) calls screaming at you on the phone, what will you do? With a liability insurance policy, the insurance company will pay (up to policy limits) third parties who claim they were injured or their property damaged by your product or service. If a lawsuit is threatened or filed, the insurance company will hire and pay (again, up to policy limits) a lawyer to defend you.

You can purchase general business liability insurance separately or as part of a commercial package policy, which combines this coverage with other types of coverages, such as property and casualty insurance. Certain small businesses, including retail outfits, can buy a business owners policy, which includes a general liability insurance line. If your business needs broader coverage or higher liability limits than these policies offer, you can purchase supplemental liability insurance with a commercial umbrella policy.

An important point: If you provide professional services (e.g., doctor, lawyer, accountant), a general liability policy doesn't cover you for losses incurred by third parties arising from your professional acts. In this case, you may need to buy professional liability insurance such as malpractice insurance, which protects you against liability for injury done to others due to your misconduct or lack of skill; or errors and omissions insurance, which protects you against liability for things that you did improperly or failed to do.

Attract and keep employees with insurance-related employee benefits

Nowadays, insurance is a crucial component of most employee benefit packages. In fact, the types of insurance that you offer (and pay for) might be a key factor in a person's decision to accept a job with you or an employee's desire to work for your business long term. Insurance helps employees feel secure, and this security can translate into loyalty and strong job performance. Here is a list of group plans that you might decide to offer as part of your employee benefits package:

- **Health Insurance**
- **Dental and vision insurance**
- **Life insurance**
- **Disability insurance**
- **Long-term care insurance**

In each case, the employee receives all of the benefits under the policy.

Transferring Your Family Business

As a business owner, you're going to have to decide when will be the right time to step out of the family business and how you'll do it. There are many estate planning tools you can use to transfer your business. Selecting the right one will depend on whether you plan to retire from the business or keep it until you die.

Perhaps you have children or other family members who wish to continue the business after your death. Obviously, you'll want to transfer your business to your successors at its full value. However, with income, gift, and potential estate taxes, it takes careful planning to prevent some (or all) of the business assets from being sold to pay them, perhaps leaving little for your beneficiaries. Therefore, business succession planning must include ways not only to ensure the continuity of your business, but also to do so with the smallest possible tax consequences.

Some of the more common strategies for minimizing taxes are explained briefly in the following sections. Remember, none are without drawbacks. You'll want to consult a tax professional as well as your estate planning attorney to explore all strategies.

You and your estate may get some relief under the Internal Revenue Code

If you are prepared to begin transferring some of your business interest to your beneficiaries, a systematic gifting program can help accomplish this while minimizing the gift tax liability that might otherwise be incurred. In 2016, you can give up to $14,000 per year, per recipient without incurring gift tax (unchanged from 2015). By transferring portions of your business in this manner, over time you may manage to transfer a significant portion of your business free from gift tax. Clearly, the disadvantage of relying solely on this method of transferring your business is the amount of time necessary to complete the transfer of your entire estate.

In addition, Section 6166 of the Internal Revenue Code allows any estate taxes incurred because of the inclusion of a closely held business in your estate to be deferred for 5 years (with interest-only payments for the first four years), and then paid in annual installments over a period of up to 10 years. Installment payments include both principal and interest. This allows your beneficiaries more time to raise sufficient funds or obtain more favorable interest rates. The business must exceed 35 percent of your gross estate and must meet other requirements to qualify.

Selling your business interest outright

When you sell your business interest to a family member or someone else, you receive cash (or assets you can convert to cash) that can be used to maintain your lifestyle or pay your estate taxes. You choose when to sell--now, at your retirement, at your death, or anytime in between. As long as the sale is for the full fair market value (FMV) of the business, it is not subject to gift tax or estate tax. But if the sale occurs before your death, it may be subject to capital gains tax.

Transferring your business interest with a buy-sell agreement

A buy-sell agreement is a legal contract that prearranges the sale of your business interest between you and a willing buyer.

A buy-sell agreement lets you keep control of your interest until the occurrence of an event that the agreement specifies, such as your retirement, disability, or death. Other events like divorce can also be included as triggering events under a buy-sell agreement. When the triggering event occurs, the buyer is obligated to buy your interest from you or your estate at the FMV. The buyer can be a person, a group (such as co-owners), or the business itself. Price and sale terms are prearranged, which eliminates the need for a fire sale if you become ill or when you die.

Remember, you are bound under a buy-sell agreement: You can't sell or give your business to anyone except the buyer named in the agreement without the buyer's consent. This could restrict your ability to reduce the size of your estate through lifetime gifts of your business interest, unless you carefully coordinate your estate planning goals with the terms of your buy-sell agreement.

Grantor retained annuity trusts or grantor retained unitrusts

A more sophisticated business succession tool is a grantor retained annuity trust (GRAT) or a grantor retained unitrust (GRUT). GRAT/GRUTs are irrevocable trusts to which you transfer appreciating assets while retaining an annuity or unitrust payment for a set period of time. In general, an annuity means you receive fixed periodic payments, while a unitrust means you receivepayments of a fixed percentage of trust assets (revalued annually). At either the end of the payment period or your death, the assets in the trust pass to the other trust beneficiaries (the remainder beneficiaries). The value of the retained annuity or unitrust interest is subtracted from the value of the property transferred to the trust (i.e., a share of the business), so if you live beyond the specified payment period, the business may be ultimately transferred to the next generation at a reduced value for estate tax or gift tax purposes.

Private annuities

A private annuity is the sale of property in exchange for a promise to make payments to you for the rest of your life. Here, you transfer complete ownership of the business to family members or another party (the buyer). The buyer in turn makes

an unsecured promise to make periodic payments to you for the rest of your life (a single life annuity) or for your life and the life of a second person (a joint and survivor annuity). A joint and survivor annuity provides payments until the death of the last survivor; that is, payments continue as long as either the husband or wife is still alive. Again, because a private annuity is a sale and not a gift, it allows you to remove assets from your estate without incurring gift tax or estate tax.

Until recently, exchanging property for an unsecured private annuity allowed you to spread out any capital gain realized, deferring capital gains tax. However, this tax benefit has generally been eliminated. If you're considering a private annuity, be sure to talk to a tax professional.

Self-canceling installment notes

A self-canceling installment note (SCIN) allows you to transfer the business to the buyer in exchange for a promissory note. The buyer must make a series of payments to you under that note. A provision in the note states that at your death, the remaining payments will be canceled. SCINs provide for a lifetime income stream and avoidance of gift tax and estate tax similar to private annuities. Unlike private annuities, SCINs give you a security interest in the transferred business.

Family limited partnerships

A family limited partnership can also assist in transferring your business interest to family members. First, you establish a partnership with both general and limited partnership interests. Then, you transfer the business to this partnership. You retain the general partnership interest for yourself, allowing you to maintain control over the day-to-day operation of the business. Over time, you gift the limited partnership interest to family members. The value of the gifts may be eligible for valuation discounts as a minority interest and for lack of marketability. If so, you may successfully transfer much of your business to your heirs at significant transfer tax savings.

What makes up my taxable estate?

Answer:

Your gross estate for federal estate tax purposes includes:

- All property that you own at death (e.g., real estate, investments, business interests, personal property, mortgages held by you)
- Property you have given away while retaining a lifetime interest in the income from the property, the use and enjoyment of the property, or the right to determine who ultimately receives the property
- Gifts that don't take effect until you die
- Property that you own jointly with another person except to the extent the other party contributed to the purchase price of the property
- Property over which you possess a general power to appoint the property to yourself or others
- Life insurance policies owned by you or in which you retained the right to change the beneficiary, cancel the policy, or make policy loans
- Your one-half interest in community property
- Annuities, pensions, and profit-sharing plans

From your total gross estate, your estate may take deductions for funeral expenses, administration expenses (e.g., executor's fees, court costs, attorney's fees, appraiser's fees), certain debts and income taxes, state death taxes paid, and property left to your U.S. citizen spouse or to qualified charities.

The net amount may be subject to estate taxes. However, the amount of taxes payable on your taxable estate may be reduced by the unified credit and a credit for foreign death taxes.

Retirement Planning Options for Business Owners

Perhaps you are self-employed or own a small business. Or, you may be directly involved in running a corporation or a tax-exempt organization. In any of these cases, you generally have the option of establishing a retirement plan in which you and/or your employees may participate. One of the main advantages of a retirement plan is that it promotes regular savings for the future. Having a good plan can also help you to attract and retain quality employees, and to maximize employee productivity. In addition, in the case of qualified plans and some nonqualified plans, a retirement plan can provide significant tax benefits for both employer and employee. These benefits may include tax-deductible employer contributions, and a tax deferral for employees until funds are distributed from the plan.

From your perspective as an employer, the challenge is finding the right plan. There are many different types of retirement plans to choose from, and each has unique features that are appropriate for some employers but not others. It is important that you select and implement the plan that best suits your needs, the needs of your business, and the needs of your employees.

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Retirement plans most appropriate for self-employed/sole proprietorship/partnership

If you are a self-employed individual or a small business owner, you know that your needs differ from those of large employers. Accordingly, there are several types of retirement plans that are specifically designed for your situation. Consider setting up one of the following types of plans: Payroll deduction IRA, Simplified employee pension (SEP), SIMPLE IRA, SIMPLE 401(k), Individual 401(k), or a Keogh plan (a qualified retirement plan established by a self-employed individual or partnership).

Retirement plans most appropriate for corporations

If you are involved with a corporation, your business may have multiple employees. One of your goals in choosing a retirement plan may be to balance their needs against the needs of your business. There are many types of plans that may enable you to achieve this goal, including the following: Payroll deduction IRA, Simplified employee pension (SEP), SIMPLE IRA , SIMPLE 401(k), 401(k), Profit-sharing, Money purchase pension, Age-weighted profit-sharing, New comparability, Thrift/savings , Defined benefit, Target benefit, Cash balance, or a Employee stock ownership plan (ESOP)

Retirement plans for tax-exempt organizations

As the name indicates, a tax-exempt organization is not subject to federal income tax. Because of this special treatment, such an organization has unique considerations for setting up a retirement plan. (For example, an employer tax deduction is generally of little or no value.) There are two types of plans that may meet the needs of tax-exempt organizations: 403(b) plans and 457(b) plans.

In addition, tax-exempt organizations may adopt a qualified retirement plan (including 401(k), profit-sharing, money purchase, and defined benefit plans). For more information, including links to detailed discussions of each type of plan, see our separate topic discussion, Retirement Plans for Tax-Exempt Organizations.

Nonqualified deferred compensation plans

You might also consider setting up a nonqualified deferred compensation plan. Compared to qualified plans, these plans are relatively flexible in that they need not satisfy stringent requirements. You and your employees may also receive more benefits under a nonqualified plan, since there are no limits on employer contributions. However, the main disadvantages of nonqualified plans are (a) they are typically not as beneficial from a tax standpoint, (b) they are generally available only to a select group of employees, and (c) the assets are not protected in the event of the employer's bankruptcy. For this reason qualified plans usually appeal to the largest number of employers and employees.

If you are an owner and wish to be included under the plan, a nonqualified deferred compensation plan will be suitable only if your business is a regular or C corporation.

Retirement plans for tax-exempt organizations

A stock plan is a form of employee compensation that provides your employees with either stock or an amount of cash that is based on the performance of your company's stock. There are numerous types of stock plans that you can offer to your employee, including employee stock ownership plans (ESOPs), restricted stock plans, stock appreciation rights (SARs), stock option plans, and employee stock purchase plans.

Self Employed Benefit Plans

As a self-employed individual, you are treated as a sole proprietor (i.e., you and your business are one and the same for tax purposes). Unlike the situation where your business is organized as a legal entity (e.g., a corporation or a partnership), if your business is operated as a sole proprietorship, you cannot be treated as an employee of your business. This can make a significant difference when it comes to establishing employee benefit plans.

Benefit plans for employees

A sole proprietorship can establish employee benefit plans for its employees that are identical to those that can be established by a corporation. Your ability to deduct the cost of such benefit plans is not affected by the fact that you are a sole proprietor, and the tax consequences to your employees are identical.

Using employee benefit plans to your own advantage

If you are a sole proprietor, your ability to personally take advantage of your business's employee benefit plans is severely limited. Why? Because you're not an employee with respect to your sole proprietorship. Therefore, most of the tax advantages associated with implementing employee benefit plans will not apply to benefits you receive individually from your sole proprietorship.

Retirement benefit plans

Although, generally, the tax benefits of employee benefit plans are not available to sole proprietors, this is not the case with employer-sponsored retirement plans. You are free to establish a retirement plan if you are self-employed regardless of whether or not you have employees, and you are completely free to participate in the retirement plan. However, if your proprietorship does have employees, you will probably have to include them in any retirement plan you establish for the business.

Other employee benefits you receive are generally not deductible

Generally, the cost of employee benefits, can be deducted by a business. However, if you are self-employed, you may be unable to take deductions for the cost of such benefits yourself or your deductions may be limited. This is true even if you provide similar benefits to your employees and are able to deduct the cost of these benefits.

An important exception is that if you are self-employed and you have a net profit for the year, you may be able to deduct, as an adjustment to income (i.e., "above the line"), up to 100 percent of the amount paid for medical and qualified long-term care insurance (subject to certain limitations) on behalf of yourself, your spouse, and your dependents.

Further, you may be able to deduct certain employee benefit costs incurred by your sole proprietorship that don't qualify as business expenses on your Schedule A. For example, the cost of medical benefits that the proprietorship pays for your own benefits might be deducted as medical expenses on your Schedule A. However, if you deduct such expenses as itemized deductions on Schedule A, the medical expense deductions are only allowed to the extent that they exceed 10 percent of your adjusted gross income, and total itemized deductions may also be limited depending on adjusted gross income.

What should I do if I determine that my income during retirement won't be enough to meet my retirement expenses?

In some cases, the best solution is to cut back current expenses and use that money toward retirement. This will enable you to put more money into your IRA, 401(k), and other retirement savings vehicles. Although you may not think you spend much on dining out and entertainment, such expenses really add up over time. Eliminating large purchases like boats and other luxury items will also make a big difference.

But if you are not able to afford to save any more than you already are, consider investing more aggressively. Weight your portfolio more heavily toward stocks and growth mutual funds, and less toward fixed-income securities. A more aggressive investment portfolio exposes you to heightened volatility, but it may also provide a much greater return over the long run.

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