

Entrepreneurs have many questions and concerns when starting a business, not the least of which is related to minimizing their legal liability. In many cases, operating a business as a Limited Liability Company, more commonly known as an LLC, may be the best way to limit the liability for both the business and owner(s) and provide tax benefits as well. (Some other entity choices include a proprietorship, partnership, or corporation.)

An LLC combines the limited liability of a corporation with the flexibility of a partnership, while avoiding the limitations on ownership and single class of stock rules applicable to S corporations. An LLC with more than one member is taxed as a partnership for federal income tax purposes unless it elects to be taxed as a corporation. This allows the members to allocate income and loss in any manner that has substantial economic effect. While enjoying this flexibility is normally available only to partnerships, LLCs also offer their members limited liability with respect to almost all LLC debts. However, a member in a professional LLC is still liable for his or her own misconduct and for the misconduct of anyone he or she supervises.

## Operating a Business as an LLC

A single-member LLC is disregarded as an entity separate from its owner for tax purposes, or it can elect to be taxed as a corporation. A business conducted in a disregarded entity (DE) owned by an individual is taxed as a sole proprietorship. A business conducted in a DE owned by a corporation, partnership, or another LLC is treated as a branch or division of the owner. Once again, there is no separate entity taxation.



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LLCs offer limited liability equal to that provided by corporations. This means members of an LLC generally are not liable for its debts or liabilities. By way of comparison, at least one partner must be a general partner who is liable without limitations for the debts of a limited partnership. As with a corporate shareholder or limited partner, the LLC member's liability to the LLC itself is generally limited to any required but unpaid capital contributions.

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The information contained in this newsletter was not intended or written to be used and cannot be used for the purpose of (1) avoiding tax-related penalties prescribed by the Internal Revenue Code or (2) promoting or marketing any tax-related matter addressed herein.

# Tax Calendar

**J**anuary 17—Individual taxpayers' final 2011 estimated tax payment is due unless Form 1040 is filed by January 31, 2012, and any tax due is paid with the return.

January 31—Give your employees their copies of Form W-2 for 2011. If an employee agreed to receive Form W-2 electronically, have it posted on the website and notify the employee.


—Give annual information statements to recipients of certain payments you made during 2011. You can use the appropriate version of Form 1099 or other information return. Form 1099 can be filed electronically with the consent of the recipient.

February 28—The government's copy of Form 1099 series returns (along with the appropriate transmittal form) should be sent in by today.

However, if these forms will be filed electronically, the due date is extended to April 2.

February 29—The government's copy of Form W-2 series returns (along with the appropriate transmittal form) should be sent in by today. However, if these forms will be filed electronically, the due date is extended to April 2.

—File Form W-3 (Transmittal of Wage and Tax Statements) along with Copy A of all the Forms W-2 you issued for 2011. If you file Forms W-2 electronically, your due date will be extended to April 2.

March 15—2011 income tax returns must be filed or extended for calendar-year corporations. If the return is not extended, this is also the last day for calendar-year corporations to make 2011 contributions to pension and profit-sharing plans. 


# Higher Education Costs Continue to Escalate

**T**he cost of attending college continues to increase. The College Board ([www.collegeboard.com](http://www.collegeboard.com)) recently reported that 2011–2012 tuition and fees have risen significantly. For example, the cost for tuition and fees at private nonprofit four-year colleges and universities is up 4.5% from 2010–2011 to an



average of \$28,500. Similar published costs to attend for-profit institutions are up 3.2% from last year to \$14,487.


The College Board indicates the average cost to attend public four-year colleges and universities is up 8.3% from last year to \$8,244 for in-state tuition and fees. For out-of-state students, the cost is up 5.7% to an average of \$20,770. Tuition and fees costs at public two-year colleges are up 8.7% to an average of \$2,963.

On the bright side, the College Board indicates subsidies provided to students through the combination of education tax credits and deductions increased to an estimated \$14.8 billion in 2010–2011. 

# Operating a Business as an LLC

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LLCs have an important asset protection advantage over corporations. A member's creditors generally cannot gain full ownership of the member's LLC interest. Instead, a creditor may be able to obtain a charging order, which conveys the right

to receive distributions. But other ownership attributes, such as the right to vote or sell the LLC interest to satisfy the creditor's claims, normally are not available to the creditor. In contrast, creditors of a shareholder can generally obtain full ownership of the stock, usually without any restrictions on the ability to vote or sell the stock. 

**S**ocial security retirement benefits are reduced when drawn before an individual reaches full benefit retirement age. As background, most social security retirement benefits are based on a worker's primary insurance amount (PIA). The PIA is based on an individual's taxable earnings averaged over the worker's lifetime to yield a monthly benefit that is designed to partially replace the earnings benefit lost because of retirement, disability, or death.

A fully insured individual can start receiving social security retirement benefits as early as age 62. However, the full benefit will be permanently reduced for each month before the individual reaches his or her full benefit retirement age (66 in 2012). Thus, the monthly benefits at age 62 will be significantly less than the benefits would have been at the full benefit retirement age.

**Example: Drawing benefits before reaching the full benefit retirement age.**

John reached age 62 in January and wants to retire. His PIA, based on his earnings history, is \$1,100 per month, and his full benefit retirement age is 66. If he retires at age 62, his monthly benefit will be reduced by 25% to \$825 per month ( $.75 \times \$1,100$ ). If he waits until his full benefit retirement age, he will receive \$1,100 per month (adjusted for inflation).

The full retirement benefit for a spouse (or divorced spouse) is generally 50% of the retired worker's PIA. However, a retiree spouse who qualifies for social security benefits based on his or her own earnings record is entitled to receive his or her own retirement benefits, if greater. If the spouse receives benefits before reaching the full benefit retirement age, the spouse's benefit is reduced based on his or her birth date. The reduction in benefits is permanent. However, if only one spouse is retired and drawing benefits based on his or her earnings, the benefits may be increased when the other spouse retires.

## Receiving Social Security Benefits before Full Retirement Age


**Example: Increasing retired spouse's benefits when the other spouse retires.**

John and Joan are married and are entitled to social security benefits based on their individual



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earnings. Both John and Joan turn age 62 this year. Joan decides to retire and her PIA is \$500, so that amount will be reduced by 25% and she will receive monthly benefits of \$375. Four years later, John retires at his full benefit retirement age, and he receives a monthly benefit equal to his PIA of \$1,100. Joan's monthly benefit will increase to \$550 based on 50% of John's benefit (the greater of Joan's \$375 PIA or 50% of John's \$1,100 PIA).

The full surviving spouse's benefit (payable if the surviving spouse or surviving divorced spouse is at least the full benefit retirement age) is 100% of the deceased spouse's PIA. However, the surviving spouse can elect to receive reduced benefits beginning as early as age 60 (50, if disabled). The reduction factor is based on the surviving spouse receiving 71.5% (a reduction of 28.5%) of the deceased worker's PIA if the surviving spouse begins drawing at age 60. The benefits are decreased for each month between the month benefits begin and the month the surviving spouse would reach full benefit retirement age. If the surviving spouse is disabled, however, the maximum reduction is still 28.5%, even if the disabled spouse begins receiving benefits at age 50. 

# 2012 Retirement Contribution and Other Limitations

The IRS recently announced cost-of-living adjustments affecting the dollar limitations



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for retirement plans, deductions, and other items. Some of the limitations will increase for 2012 because the increase in the cost-of-living index met the statutory

threshold. However, many limitations did not meet that threshold and remain unchanged from 2011.

The elective deferral (contribution) limit for employees who participate in 401(k), 403(b), most 457 plans, and the federal government's Thrift Savings Plan increased from \$16,500 in 2011 to \$17,000 in 2012. The catch-up contribution limit for those aged 50 and over remains unchanged at \$5,500.

You can contribute up to \$5,000 (\$6,000 if you are age 50 or older by year-end) to your IRA in 2012 if certain conditions are met (i.e., sufficient earned income). The IRA contribution limit is unchanged from 2011. For married couples, the combined contribution limits are \$10,000 (\$5,000 each) and \$12,000 (\$6,000 each if both

are age 50 by year-end) when a joint return is filed, provided one or both spouses had at least that much earned income. Keep in mind that contributions to traditional IRAs may be tax-deductible, subject to specific limitations that increase for 2012.

When you establish and contribute to a Roth IRA, contributions are not deductible, but withdrawals are tax-free when specific requirements are satisfied. In addition, there are no mandatory distribution rules at age 70½ with a Roth IRA, and you can continue to make contributions past age 70½ if you meet the earned income requirement.

The 2012 limitation for SIMPLE retirement accounts remains unchanged at \$11,500. Likewise, the SIMPLE catch-up contribution for those age 50 by year-end is unchanged from 2011 at \$2,500.

The 2012 contribution limit for profit-sharing, SEP, and money purchase plans is the lesser of (1) 25% of the employee's compensation—limited to \$250,000, an increase of \$5,000 from 2011 or (2) \$50,000, an increase of \$1,000 from 2011.

The social security wage base for computing the social security tax (OASDI) increases to \$110,100 in 2012, up from the \$106,800 wage base for 2011. The additional \$3,300 for 2012 represents an increase of about 3% in the wage base.

Finally, the annual exclusion for gifts remains unchanged at \$13,000 in 2012.

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