WHAT THE NEW TAX LAW MEANS FOR YOU

HOW TO MAXIMIZE YOUR VALUE AS A FINANCIAL ADVISOR AND BUSINESS OWNER UNDER THE NEW TAX LAW

The contents of this document are for educational purposes only and do not constitute tax advice. The tax related information in this document were prepared, reviewed, and approved by an independent Public Accounting CPA firm. LPL Financial does not give tax or legal advice. Individuals should consult with their own attorney or tax advisor regarding their specific situation.
The Tax Cuts and Jobs Act of 2017 is the first significant makeover to the tax code in over 30 years. But what do these changes mean for you and your business? Is now the right time to pursue an independent practice or restructure an existing one? There’s a lot to think about as you weigh your options under this new tax regime, and ensuring that you have the right resources and support will help you make the best decisions for your future.
A favorable business climate and lower tax rates on business income offer unprecedented opportunities for independent advisors and practices of all sizes. The first step to reaping those benefits is understanding the implications of the recently enacted tax legislation. As you seek to grow, protect, and lock down future value in your business, here’s what you need to know about opportunities available under the new tax law.

**KEY TAX PROVISIONS IMPACTING YOUR BUSINESS**

One of the most significant changes impacting advisors under the new tax law is the limiting of an employee’s unreimbursed business expense deductions. For W-2 advisors at wirehouses and regional firms, as well as salaried advisors at independent practices, the loss of these deductions can significantly increase the costs of doing business. Because deductions for continuing education credits, association memberships, home office costs, publications, mileage, entertainment, and other expenses have been eliminated, many W-2 advisors will find themselves at a distinct disadvantage compared with their independent business owner peers.

With the exception of entertainment expenses, nonemployee business owners will continue to deduct these and other business expenses in addition to potentially benefiting from the new lower tax rates on business income.

The new tax law contains two key provisions aimed at helping business owners keep more of the income they generate:

- **Deduction for pass-through business entities:** Beginning in 2018, the new rules include a tax deduction for owners of pass-through entities, including partners in partnerships, shareholders in S corporations, members of limited liability companies (LLCs) and sole proprietors.

- **21% corporate tax rate:** The new tax law provides a permanent 21% rate on business income generated by corporations. The new flat rate is a significant reduction from the previous top corporate tax bracket of 35%.

The contents of this document are for educational purposes only and do not constitute tax advice. The tax-related information in this document was prepared, reviewed, and approved by an independent Public Accounting CPA firm.
THE BENEFITS OF BUSINESS OWNERSHIP

Preferential tax treatment is only one of many reasons financial advisors seek business ownership. The ability to create business equity and monetize their practices remains the leading reason advisors seek independence.¹ As an employee-advisor, you create value for your firm, but don’t share in that equity appreciation over time. As a business owner, all equity appreciation goes to you. That enables you to create something of value that can be monetized when you’re ready to sell or exit the business.

Business ownership also allows you to conduct business in the way that makes the most sense for you—that addresses your financial goals and best leverages your skills. Just as importantly, independence allows you to serve your clients in the manner that is in their best interest, with the advice, investments, and services that you determine are the most appropriate.

While taxes are a leading consideration for how to structure your business, they aren’t the only factor in determining the right path forward. They should be viewed in the context of your personal circumstances, as well as the goals and objectives you’ve established for your practice. That said, if you do decide to establish your own independent business, here are some important considerations.

BENEFITS OF PASS-THROUGH BUSINESS ENTITIES

Under the prior tax code, income from small nonincorporated businesses—such as partnerships, LLCs, and sole proprietorships—passed through to the owner and was subject to individual income tax rates as high as 39.6%. Under the new tax law, the top marginal income tax rate is 37% for taxpayers with taxable income of $500,000 and higher for single filers and $600,000 and higher for married couples that are filing jointly.²

The hypothetical example below illustrates how the new 20% deduction is applied—your situation will vary.

ASSUMPTIONS

- Joint filer with a Schedule C business has a standard deduction of $24,000
- Business gross income of $400,000
- Business expenses of $100,000
- Net profit from business $300,000 (qualified business income)
- Spouse works and makes $46,978
- Above-the-line deductions of $11,978 for deductible portion of self-employment tax and $20,000 for SEP IRA contribution

ANALYSIS

Taxable income before application of pass-through deduction = $291,000

In this case, the taxable income of $291,000 is less than the qualified business income of $315,000. As a result, the 20% pass-through deduction will apply to the qualified business income, resulting in a $58,200 deduction.

OUTCOME

The couple’s taxable income after application of the pass-through deduction is $232,800, placing them in the 35% tax bracket, so they save about $20,370 in federal taxes.

The above is meant as an example only. Please consult with your tax advisor for additional information.
The new 20% pass-through deduction further reduces the tax burden for certain business owners. As a result, many advisors view this as a prime opportunity to strike out on their own thanks to an opportunity to repurpose tax savings toward establishing an independent practice. However, not all advisors will benefit from the pass-through deduction, which is scheduled to sunset in 2026.

Due to restrictions placed on business owners in the professional services industries, including consultants, doctors, partners in law firms, and financial advisors, the deduction isn’t available for business owners in those industries earning more than $157,500 (single filers) or $315,000 (married couples filing jointly). For high earners in industries outside of professional services, a calculation is used to cap their deduction based on whichever is higher: 50% of total wages paid or 25% of wages plus 2.5% of the cost of tangible depreciable property.  

It’s also important to note that partners in certain industries and professions (including financial advisors) could encounter a situation where one owner or partner is able to take the 20% deduction but the other is not. For example, for a partner with a high-income spouse, the couple’s combined income could exceed the taxable income threshold of $315,000 for married couples filing jointly. In this case, it may make sense to seek the advice of a tax professional to determine if filing separately is an appropriate solution.

These limitations are an example of why it’s so important to maintain a holistic perspective when considering the right structure for your business.

**WHY INCORPORATING MAY BE BETTER FOR LONG-TERM BUSINESS GROWTH**

While most pass-through business entities are easier and less costly to establish and maintain than a corporation, if you expect to generate business income in excess of the established thresholds for the 20% pass-through deduction, incorporating your business to take advantage of the 21% corporate tax rate may be an alternative to lock in the permanent

**BUSINESS OWNERSHIP PROVIDES GREATER FLEXIBILITY**

- Write-off most direct business expenses and overhead
- Retain control over decision-making
- Choose among multiple retirement plan options, including ability to implement solo defined benefit plan
- Control cash flow
- Defer income as needed
- Determine service offering and client experience
- Choose your business location
- Own your book of business

---

3 Thomson Reuters; 2017

The contents of this document are for educational purposes only and do not constitute tax advice. The tax related information in this document were prepared, reviewed, and approved by an independent Public Accounting CPA firm.
What used to restrict business and limit small business profits now opens up a variety of opportunities for business growth.

21% tax rate. However, structuring your business as a C corporation is generally more costly due to the taxation of profits at both the corporate and personal level. C corps also have rigorous reporting requirements which can be time consuming for business owners to stay on top of and costly to outsource.

FINDING THE RIGHT SUPPORT

Today’s business-friendly economic climate offers significant opportunities for practices at all stages of business growth, from start-ups to mature practices. Potentially lower tax rates on business income translates to more cash on hand for capital expenditures and reinvestment, restructuring, hiring, M&A activity, and more. However, capitalizing on the opportunities that are right for your business requires access to deep resources. Your tax professionals can help you more fully understand how the new law may impact your business, while affiliating with the right broker/dealer can offer the additional support you need to build the practice you envision for your future.

LPL Financial’s Strategic Business Solutions team can make a difference for your business. For more than 40 years LPL Financial has helped thousands of financial advisors build and grow profitable, independent practices that establish themselves as a premier provider of investment advice in the communities they serve. If you choose LPL, the Strategic Business Solutions team serves as your value-maximizing partner, providing independent advisors access to a broad array of valuable business consulting resources and services designed to grow, protect, and lock down business equity.

These industry consultants are experienced in business development, financing, strategic sourcing, and succession planning. For decades, they have helped advisors accelerate business growth, avoid potential pitfalls, and pursue their goals. Access to dedicated resources and expertise in transition planning, business development, business valuation, M&A deal structuring, and succession planning can help practices of all sizes pursue their business goals from start-up to retirement or sale of the business.

Learn more about how LPL can offer the resources and advice to help you navigate today’s evolving industry environment and support the future growth of your business.

The contents of this document are for educational purposes only and do not constitute tax advice. The tax related information in this document were prepared, reviewed, and approved by an independent Public Accounting CPA firm.
Your Practice, Your Way

However you envision the future of your practice or program, LPL’s comprehensive support and broad range of innovative business models can help you build and grow your business, your way. LPL understands that independence doesn’t have one single meaning. Whatever lens you view your independence through, LPL is here to support and provide clarity to that vision, whether you want to:

- Be an independent financial advisor at LPL with access to custodian services and a fully integrated platform to address the varied needs of your clients.
- Leverage the LPL Hybrid RIA model, which allows you to join LPL’s broker/dealer platform while maintaining your registered investment advisor (RIA) firm.
- Join an existing practice, bank, or credit union for established infrastructure, structured support, and access to new referral sources.
- Specialize in retirement plans and leverage tools and resources built by retirement plan advisors, for retirement plan advisors.
- Bring your entire practice or build one—LPL offers customized clearing, advisory platforms, and technology solutions to help create efficiencies and scalability within your practice.

Discover how LPL Financial can help you and your practice reach your full potential. Call us at (888) 250-2420 to speak in confidence with one of our experienced recruiters, or visit us online at www.JoinLPL.com today.

LPL Financial does not give tax or legal advice. Individuals should consult with their own attorney or tax advisor regarding their specific situation. This material is not intended or written to be used, and cannot be used or relied upon, by any advisor or taxpayer for the purpose of (i) avoiding penalties under the Internal Revenue Code, or (ii) promoting, marketing, or recommending to another party any transaction(s) or tax-related matter(s).

 Securities offered through LPL Financial, member FINRA/SIPC. Insurance products offered through LPL Financial or its licensed affiliates.

<table>
<thead>
<tr>
<th>Not FDIC/NCUA Insured</th>
<th>Not Bank/Credit Union Guaranteed</th>
<th>May Lose Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not Guaranteed by Any Government Agency</td>
<td>Not a Bank/Credit Union Deposit</td>
<td></td>
</tr>
</tbody>
</table>

About LPL

LPL Financial is one of the nation’s leading financial services companies and a publicly traded company under ticker symbol LPLA. The firm’s mission is rooted in the belief that objective financial guidance is a fundamental need for everyone. LPL does not offer proprietary investment products or engage in investment banking activities; this means advisors affiliated with LPL are not pressured or influenced by LPL to sell its products. Thousands of financial advisors nationwide are able to rely on the firm’s tools and resources to help them provide financial guidance and recommendations to address their clients’ needs. For more information about LPL Financial, visit www.lpl.com.

LPL Financial, a registered investment advisor, member FINRA/SIPC
BD-20531-0218 Tracking #1-703487 (Exp. 3/19)