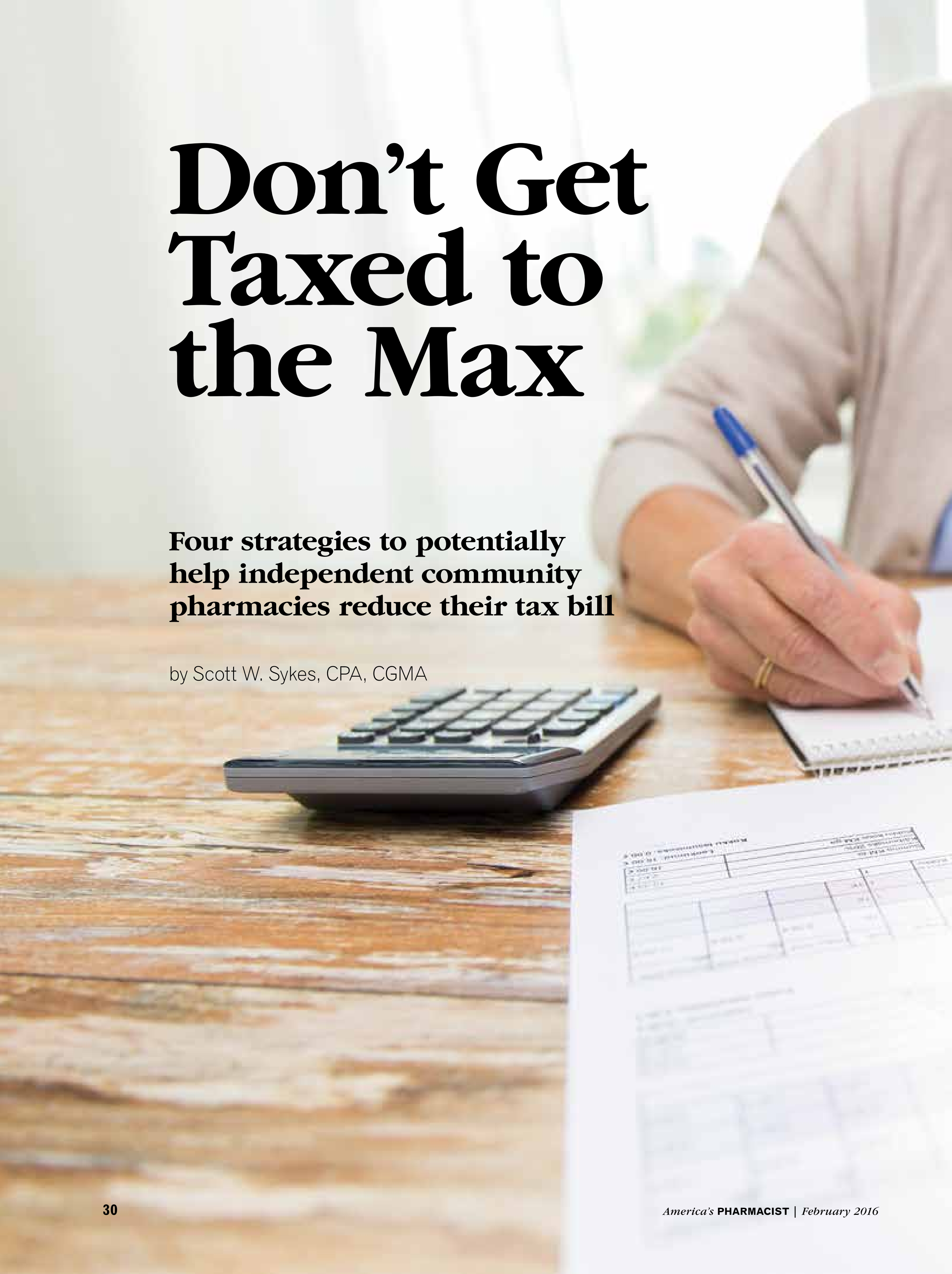
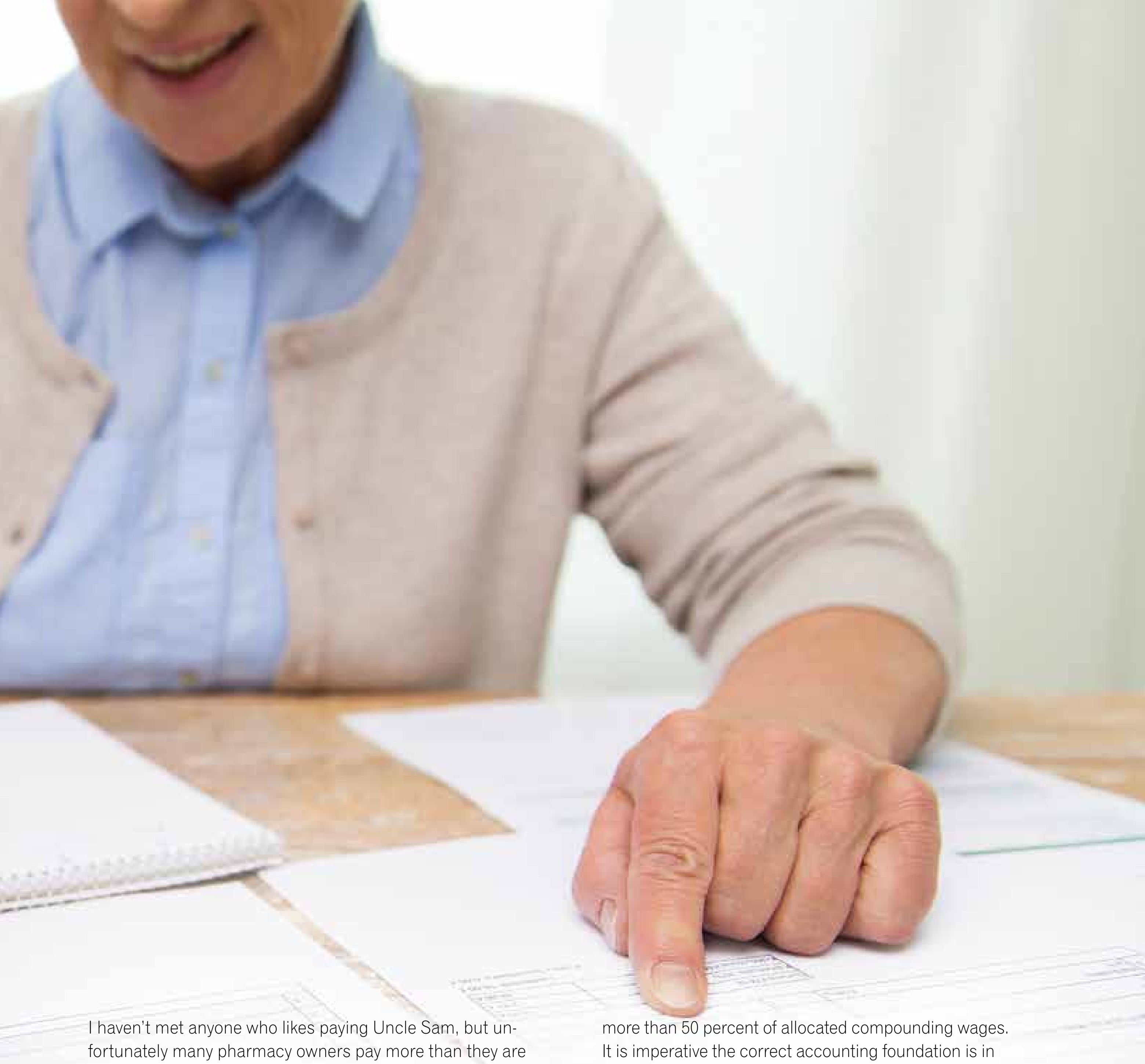


Don’t Get Taxed to the Max

Four strategies to potentially help independent community pharmacies reduce their tax bill

by Scott W. Sykes, CPA, CGMA



I haven't met anyone who likes paying Uncle Sam, but unfortunately many pharmacy owners pay more than they are legally required to do. If you're like most pharmacy owners, you fall into the top tax rates of 39 percent plus state tax rates. With cash flow tight in many pharmacies, these four strategies may improve your situation. You may not qualify or they may not fit your goals, but they're worth discussing with your advisors.

- **Domestic Production Deduction.** The Internal Revenue Code (IRC) Section 199 covers the domestic production deduction, which applies to U.S.-based manufacturers. Under current law, pharmacies that produce revenues from compounding services may qualify for this deduction. Although complex to calculate, the deduction can be as much as 9 percent of qualified production activities income or your adjusted gross income, not to exceed more than 50 percent of allocated compounding wages. It is imperative the correct accounting foundation is in place to maximize your benefit from this deduction.

- **Section 179 Depreciation.** Waiting until the very last minute of 2015, lawmakers passed the Protecting Americans from Tax Hikes (PATH) Act of 2015. The PATH Act retroactively restored for 2015 and 2016 the $500,000 Section 179 depreciation deduction and extended it permanently. Section 179 provides a current "expensing" deduction for qualified business property placed in service during the year. This is particularly important if you are in need of some technology updates in your pharmacy. For example, a $250,000 robot put in place and in use in 2015 or 2016 would be able to be written off, which will save you about 40 percent in taxes, or $100,000. Keep in mind however, the deduction cannot exceed the net taxable income from all the businesses actively operated by the taxpayer, it must be in "use" before the end of the year and new equipment purchases are phased out at $2 million, indexed for inflation.

- Conservation Easements. Conservation easements provide limits on how land is used, for purposes such as wildlife preservation. They are a one-time charitable deduction and are currently limited to 50 percent of your adjusted gross income (AGI) with any excess allowed to carry forward. A taxpayer can invest in one of these easement entities and they usually get about a four or five to one deduction for the year, depending on the appraisal. This is a highly complex area of the tax law, but one that can provide benefits to the taxpayer that is considerable. In some cases this may greatly reduce or eliminate your tax bill for the year. Conservation easement investments usually carry high setup expenses and are not for every taxpayer, but they do offer an alternative.

- Various Retirement Options. Older pharmacy owners with limited debt and a plan in place to retire in the next 5-10 years should inquire about a more powerful retirement plan such as a cash-balance option. Although there can be higher in fees to set up and manage, the benefits of stashing away thousands of dollars into a tax deferred account far outweigh the fees. Some plans, when put into place, can completely wipe out all taxable income with most of the contributions going to the pharmacy owners and family members employed by the pharmacy.

As with any tax strategy, perform your due diligence and discuss these options with your CPA or advisor before making any decisions, as strategies mentioned above are subject to change with Congressional action. It is also imperative that the pharmacy has a solid accounting foundation in place. Without that, you may be missing basic strategies.

You can think of a well-tuned accounting foundation as working like a high end sports car. Its precision steering and power allows you to take control of your destiny with proactive tax planning and management decisions. And that speeds you down the road to fulfilling your goals, needs and desires. ■

Scott W. Sykes, CPA, CGMA is with Sykes & Company, P.A., working directly with pharmacy owners, assisting with day to day accounting and tax compliance issues. He is also active in year-end payroll preparation, tax planning, individual tax preparation and corporate tax preparation for pharmacy owners and businesses.