

LAW FIRM & LEGAL NEWSLETTER

Thaney & Associates, CPAs Monthly Company Newsletter



Summer Client Update Newsletter

The last thing you may want to do during the summer is start thinking about your 2022 tax return! The best way to lower your tax bill for next year, however, is to start looking for tax cutting strategies as soon as possible.

In this month's newsletter, read about some tax planning tips to help you lower your 2022 taxes. Also read about tax implications if you have a side hustle, and money management tips for couples!

Please feel free to forward the information to someone who may be interested in a topic and call with any questions you may have.

THANEY & ASSOCIATES
— Certified Public Accountants —

IN THIS ISSUE

START YOUR TAX PLANNING NOW!

HUSTLING FOR EXTRA INCOME! (DON'T FORGET THE TAXMAN)

5 GREAT THINGS ABOUT IRA

MONEY MANAGEMENT TIPS FOR COUPLES

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Start your Tax Planning NOW!

Keeping your taxes as low as possible requires paying attention to your financial situation throughout the year. Here are some tips for getting a head start on tax planning for your 2022 return:

Check your paycheck withholdings. Now is a good time to check your tax withholdings to make sure you haven't been paying too much or too little. The IRS has an online tool that will help you calculate how much your current withholdings match what your final tax bill will be. Visit <https://apps.irs.gov/app/tax-withholding-estimator>.

Action step: To change how much is withheld from your paycheck in taxes, fill out a new Form W-4 and give it to your employer.

Defer earnings. You could potentially cut your tax liability by deferring your 2022 income to a future year via contributions to a retirement account. For 2022, the 401(k) contribution limit is \$20,500 (\$27,000 if 50 or older); \$6,000 for both a traditional and Roth IRA (\$7,000 if 50 and older); or \$14,000 for a SIMPLE IRA (\$17,000 if 50 and older).

Action step: Consider an automatic transfer from either your paycheck or checking account to your retirement account so you won't have to think about manually making a transfer each month

Plan withdrawals from retirement accounts to be tax efficient. Your retirement accounts could span multiple account types, such as traditional retirement accounts, Roth accounts, and taxable accounts like brokerage or savings accounts. Because of this you should plan for your withdrawals to be as tax efficient as possible.

Action step: One way to structure withdrawals is to pull from taxable accounts first, and leave Roth account withdrawals for last. Another approach would be to structure proportional withdrawals from all retirement accounts that would lead to a more predictable tax bill each year..

Net capital gains with capital losses. If you have appreciated investments you're thinking about selling, take a look through the rest of your portfolio to see if you have other assets that you could sell for a loss and use to offset your gains. Using the tax strategy of tax-loss harvesting, you may be able to take advantage of stocks that have underperformed.

Action step: Make an appointment with your investment advisor to look over your portfolio to see if there are any securities you may want to sell by the end of 2022.

LAW FIRMS & LEGAL SERVICES IN THE US

Executive Summary

Law abiding: Strengthening business activity and corporate profit will likely help drive growth

Operators in the Law Firms industry range from sole practitioners to large, full-service legal firms mostly serving corporate clients. Industry revenue growth has been modest over the five years to 2022. Although the industry benefited from economic growth through most of the period, it was negatively affected by the COVID-19 (coronavirus) pandemic in 2020. Overall, industry revenue is expected to increase at an annualized rate of 1.3% to \$367.9 billion during the current period, including an increase of 1.9% in 2022 alone.

Greater demand for practices tied to high-growth sectors has boosted industry revenue over the past five years. Industry revenue growth has been primarily due to growth in demand for litigation, intellectual property and merger and acquisition (M&A) services. However, as the coronavirus pandemic ravaged the economy in 2020, many operators experienced declines in revenue as downstream clients cut costs due to uncertainty and reduced demand. Nonetheless, revenue declines were mitigated by services that run countercyclical to the economy.

Industry revenue is forecast to increase an annualized 1.2% to \$390.2 billion over the five years to 2027 largely due to stronger economic performance. An increasing number of mergers and acquisitions (M&As), coupled with heightened initial public offering (IPO) activity and broad-based economic growth, is expected to support revenue growth for the industry over the five years to 2027. Delayed business activities requiring legal services, such as capital raisings, will likely resume over the next five years, while rising disposable income is expected to aid smaller operators by increasing demand for services such as family law. In addition, improving investor confidence will likely stimulate more activity in IPO markets, facilitating higher demand for corporate legal services.



For example, an uptick in bankruptcy filings and labor and employment disputes related to the economic downturn helped ameliorate the overall economic contraction. In particular, demand from the private equity and M&A markets bolstered revenue for top firms in 2020. Industry profit remained stable overall during the five-year period as declines in revenue have been offset by reduced costs as a result of remote work by law firms. In 2022, the industry as a whole is expected to benefit from broad-based economic growth and resumption in spending by downstream businesses and households.

Hustling for Extra Income

Don't forget the taxman!

From supplementing their current income to replacing income that was lost because of layoffs, the pandemic or other reasons, many people have started side hustles over the past 2 years to help make ends meet.

If you currently have a side hustle, don't forget about the tax implications from earning extra money. Here are several ideas to help you stay on top of your side hustle's taxes:

- **All income must be reported.** Income from side hustles can come from a variety of sources. Regardless of where the money comes from or how much it is, it is supposed to be reported on your tax return. If you do work for a company, expect to receive a 1099-NEC or 1099-MISC if you are an independent contractor, or a W-2 if you're an employee.
- **Keep good records and save receipts.** Being organized and having good records will do two things: ensure accurate tax reporting and provide backup in the event of an audit. Log each receipt of income and each expense. Save copies of receipts in an organized fashion for easy access. There are multiple programs and apps to help with this, but a simple spreadsheet may be all that you need.
- **Don't fall into the hobby trap.** You won't be allowed to deduct any expenses if the IRS determines that your side hustle is a hobby instead of a business. To make sure your side hustle is deemed a business by the IRS, you should show a profit during at least three of the previous five years.
- **Get professional tax help.** There are many other tax factors that can arise from side income such as business entity selection, sales taxes, state taxes, and more. Please call to set up a time to work through your situation and determine the best course of action for your side hustle.

- **Make estimated payments.** If you are running a profitable side business, you will owe additional taxes. In addition to income tax, you might owe self-employment tax as well. Federal quarterly estimated tax payments are required if you will owe more than \$1,000 in taxes for 2022. Even if you think you will owe less than that, it's a good idea to set a percentage of your income aside for taxes to avoid a surprise when you file your 2022 return.



INDUSTRY OUTLOOK

Revenue for the Law Firms industry is forecast to increase at an annualized rate of 1.2% to \$390.2 billion over the five years to 2027.

A projected increase in corporate profit as the economy recovers will likely drive industry demand from businesses during the outlook period. At the same time, improving investor confidence is expected to stimulate M&A and IPO activity. Specifically, the value of IPOs is expected to increase at an annualized rate of 1.1% over the five years to 2027. This increase will likely spur revenue growth for the industry's largest firms, which aid corporations in deals and equity offerings. Moreover, an increase in corporate litigation activity, which generates a sizeable share of revenue for large firms, is projected to be positive growth factor for the industry. Businesses that delayed legal issues in 2020 due to cost-cutting measures amid the COVID-19 (coronavirus) pandemic are anticipated to resume use of industry services over the next five years, boosting industry revenue. As businesses continue to be digitized and cybersecurity issues continue to remain prominent, IP litigation and technology sector antitrust and data-related litigation will continue to drive demand for industry services.

From the consumer sector, demand from households is expected to increase as employment increases and disposable incomes grow. Households will likely use industry services for estate planning, family law and litigation, among other things. Similarly, an increase in construction activity, which drives demand for industry real estate law services, is forecast to benefit the industry as private nonresidential construction activity resumes and there is continued growth in the residential construction market.



Industry operators have adopted price competition and alternative billing schedules to attract more clients and differentiate themselves from other firms.

Although downstream market improvements will likely lead to industry revenue growth over the next five years, competition and a desire to attract clients through alternative methods is expected to continue. Such practices have the potential to put downward pressure on fees, resulting in lower industry revenue. Moreover, for large firms that experienced an increase in profitability in 2020 due to reduced operating costs amid the coronavirus pandemic, downstream businesses may seek price concessions from industry operators. Increasing use of artificial intelligence to automate certain mundane and repetitive tasks that have traditionally been time-consuming may also reduce billable hours. While this could lead to a reduction in industry revenue, it will likely free up operators to spend more time on productive tasks and make legal services more cost-efficient for downstream businesses.

The industry's largest firms are expected to continue expanding overseas operations in emerging markets over the next five years.

Law firms have commonly gained a foothold in high-growth regions, such as China and Indonesia, through M&As and partnerships. In particular, more mergers and expansions into African markets are expected to take place among global firms over the next five years. Due to a combination of its size, the fact that the continent's economy is expected to grow significantly over the course of the 21st century and its deeper anticipated integration with the global economy, the region is an attractive market for M&As.

INDUSTRY OUTLOOK

The Law Firms industry provides expertise on a range of legal practices, including criminal law, business and commercial law, tax law, intellectual property and real estate.

Industry operators range from sole proprietors specializing in one particular type of law to international law firms that offer full legal services and employ upward of 3,000 attorneys. The industry's largest firms rely on commercial activities, acting as legal advisers on corporate deals, such as M&As and IPOs. Legal services tied to real estate also comprise a significant share of industry revenue. Demand for legal services has grown over the five years to 2022, in line with the overall economy. Generally strong economic performance prior to 2020 drove demand for industry services, which are mostly procyclical. As a result, industry revenue is expected to increase at an annualized rate of 1.3% to \$367.9 billion during the current period.

In 2020, however, the industry experienced a contraction amid falling corporate profit and poor economic performance caused by the COVID-19 (coronavirus) pandemic. Despite this, some services offered by industry operators are countercyclical and experience growth during economic downturns, mitigating the overall effect of recessions. As a result, industry revenue only declined an estimated 0.6% in 2020. Moreover, in 2022, rapid economic growth driven by widespread vaccination efforts and government stimulus programs is expected to benefit the industry, leading industry revenue to increase an estimated 1.9% in the year.

PROFIT & EMPLOYMENT

Industry profit, measured as earnings before interest and taxes, has increased over the past five years, accounting for an estimated 21.4% of revenue in 2022, up slightly from 20.1% in 2017.

Profit increased to an estimated 21.3% of industry revenue in 2020, even as demand for services decreased slightly due to the pandemic. However, the decline in industry profit was ameliorated by lower costs, as industry operators implemented remote work policies, effectively reducing overhead expenses and, thus, maintaining the industry's profitability. While profit as a whole was negatively affected, the largest operators in the industry benefited from increased demand for M&A and private equity market activity combined with lower costs, leading their profitability to grow in 2020. In 2022, industry profit is expected to increase, largely as a result of increasing downstream demand as the economy recovers. Although industry revenue has increased over most of the past five years, law firms have still been reluctant to hire new associates as frequently as they were willing to in the past. As a result, industry employment has remained relatively stable, rising at an annualized rate of only 0.6% to 1.4 million workers in 2022.



INDUSTRY OUTLOOK

Consolidation has also dissuaded law firms from bringing on new attorneys by permitting them to hire laterally and select from a pool of experienced professionals. As a result, competition for employment remains high among recent law school graduates because many law firms have pared back their summer associate programs and reduced or discontinued hiring of first-year associates. According to a 2020 Altman Weil survey, 5.2% of respondents indicated they would reduce hiring of first year associates, while 18.6% said they would remove underperformers from their firm. Moreover, staffing restructurings that resulted from the new, virtual work environments of law firms in 2020 have reportedly continued into early 2022.

Amid the coronavirus pandemic, this trend has further accelerated, with remote work environments and changing employment conditions necessitating the use of legal services.

Additionally, as unemployment increased in 2020 due to the coronavirus pandemic, industry operators experienced an increase in labor and unemployment cases, helping to mitigate revenue declines from other segments. In 2022, demand is expected to be driven by a resumption in spending by small businesses that were most hurt in 2020 by the coronavirus pandemic, in addition to households as consumer spending and confidence increase alongside incomes and employment.

The frequency of mega-mergers has also escalated during the period, benefiting large industry operators. For example, Skadden, Arps, Slate, Meagher and Flom LLP and associates, working on behalf of El du Pont de Nemours and Company (DuPont), reached a settlement in June 2017 with the Antitrust Division of the United States Department of Justice that permitted DuPont to merge with the Dow Chemical Company for \$130.0 billion. Additionally, Kirkland & Ellis LLP represented Bristol Myers Squibb Company in the acquisition of Celgene Corporation for \$74.0 billion. Over most of the past five years, globalization has fueled demand for cross-border M&As and provided a stable stream of revenue for multinational law firms.



REVENUE GROWTH FACTORS

Industry revenue generally increases in line with overall economic growth.

Corporate deal-making activity, which includes M&As and IPOs, has improved industry revenue during the current period, particularly for the industry's largest operators. IPOs increased significantly over the past five years, with jumps of 88.8% and 32.1% in 2017 and 2018, respectively, and increased 77.5% in 2021. An increase in this activity boosts demand for industry services because companies often require legal services to navigate the process. Further, increased intellectual property (IP) and litigation revenue as a result of the heightened digitization of businesses has driven industry revenue growth. Litigation resulting from cybersecurity and internet of things breaches has increased due to the heightened centrality of big data for business operations, while the importance of IP for tech companies has continued to drive revenue growth from that sector.

IRA

5 Great Things About IRA's

IRA's can be a powerful tool to lower taxes all while saving for retirement or other predetermined uses. Here are five fairly unreported things to know about IRA's.

A nonworking spouse can have an IRA. If your spouse doesn't work, you may still be able to open and contribute to an IRA for your spouse, assuming that you work and file a joint tax return. This can be a great way to help reduce your taxable income each year.

You may still contribute to an IRA if you have a 401(k) or similar program at work. As long as you do not exceed the income limits, it is ok to have both an IRA as well as other forms of retirement savings plans. It's simply important to know your options and plan accordingly.

Even children can have IRAs. If your child has earned income, you can open and contribute to an IRA. Just ensure you can document the earnings. While your child can contribute their own earnings, many parents will help keep track of things like babysitting money, then match those earnings in either a traditional or ROTH IRA. Often the ROTH IRA is preferred, because the future earnings could be tax free! Your child's IRA is managed by an adult until the child is old enough for the account to be transferred to their name.


Non-deductible contributions may be made. If you exceed IRA income phaseouts, contributions to your IRA may not reduce your taxable income for the year. But you may still want to make after-tax contributions to a non-deductible IRA. Remember, while you are taxed on the contributions to a non-deductible IRA, the earnings can still grow tax-deferred.

Tax rules surrounding IRAs are vast and complex. But within the rules are numerous situations that if you know they exist, can help you plan for a more tax-efficient future.

It's not just for retirement. With traditional IRAs, if you withdraw funds before the age of 59 1/2 you may be subject to income tax AND an early withdrawal penalty. But there are exceptions to this rule. These include withdrawals for a first time home purchase, major medical bills, college costs, birth/adoption and many others. However, it is important to know the rules BEFORE you withdraw the funds.

Money Management Tips for Couples

Couples consistently report finances as the leading cause of stress in their relationship. Here are a few tips to avoid conflict with your long-term partner or spouse.

-  **Be transparent.** Be honest with each other about your financial status. As you enter a committed relationship, each partner should learn about the status of the other person's debts, income and assets. Any surprises down the road may feel like dishonesty and lead to conflict.
-  **Frequently discuss future plans.** The closer you are with your partner, the more you'll want to know about the other person's future plans. Kids, planned career changes, travel, hobbies, retirement expectations — all of these will depend upon money and shared resources. So discuss these plans and create the financial roadmap to go with them. Remember that even people in a long-term marriage may be caught unaware if they fail to keep up communication and find out their spouse's priorities have changed over time.
-  **Know your comfort levels.** As you discuss your future plans, bring up hypotheticals: How much debt is too much? What level of spending versus savings is acceptable? How much would you spend on a car, home or vacation? You may be surprised to learn that your assumptions about these things fall outside your partner's comfort zone.
-  **Divide responsibilities, combine forces.** Try to divide financial tasks such as paying certain bills, updating a budget, contributing to savings and making appointments with tax and financial advisors. Then periodically trade responsibilities over time. Even if one person tends to be better at numbers, it's best to have both members participating. By having a hand in budgeting, planning and spending decisions, you will be constantly reminded how what you are doing financially contributes to the strength of your relationship.
-  **Learn to love compromising.** No two people have the same priorities or personalities, so differences of opinion are going to happen. One person is going to want to spend, while the other wants to save. Vacation may be on your spouse's mind, while you want to put money aside for a new car. By acknowledging that these differences of opinion will happen, you'll be less frustrated when they do. Treat any problems as opportunities to negotiate and compromise.

As always, should you have any questions or concerns regarding your tax situation or would like to start your tax planning; please feel free to call at 888-252-8769.