Tax topics:
Bonus depreciation extended

> "Bonus depreciation, which allows capital equipment to be written off at a faster rate beyond what the IRS Section 179 deduction allows, has been extended and applies to the first $2 million spent ... Only new equipment — not used — qualifies for accelerated depreciation."[1] – *New York Times*

Passed by Congress in January 2013, the 2012 American Taxpayer Relief Act renewed selected economic stimulus measures, including a 50-percent accelerated (bonus) depreciation for new capital asset purchases made in 2013. Bonus depreciation lets an organization use the MACRS (Modified Accelerated Cost Recovery System) – plus an additional 50 percent of tax depreciation – on 2013 tax returns.

Eligible equipment must be placed in service before December 31, 2013. For purchase contracts signed during 2013, some transportation assets with extended build times (such as vessels, rail assets and corporate aircraft) may be placed in service before the end of 2014.[2]

Is bonus depreciation beneficial?

Depending on an organization's financial profile, bonus depreciation may – or may not – offer worthwhile benefits. For instance, during the first year of ownership, bonus depreciation hastens the already quick rate of depreciation for MACRS equipment.

Faster depreciation may seem an irresistible advantage.

Initially, faster depreciation may seem an irresistible advantage: What organization wouldn't like to reduce its tax burden, especially in times of economic uncertainty? Capital equipment depreciation often represents the largest non-cash expense of a healthcare enterprise. Its power to reduce taxable income is significant, though not always advantageous.

Consider two situations in which bonus depreciation may hinder financial interests:

1. Avoid tax losses with NOLs

If neither anticipated nor well managed, excessive depreciation can lower taxable income and create a Net Operating Loss (NOL). Although NOLs can offset future taxable income, they typically take time and judicious planning to implement. Adding more depreciation (through new equipment purchases and bonus depreciation) impedes efforts to use NOLs effectively. In contrast, a tax lease can help organizations avoid adding more depreciation, which may prevent creating unnecessary NOLs – or protracting a current one.

A tax lease can prevent or curtail a Net Operating Loss.

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[1] http://www.nytimes.com/2013/02/10/business/yourtaxes/for-small-businesses-tax-law-has-become-a-moving-target.html?_r=0

[2] Consult your financial advisor for a complete list of eligibility requirements.

2. Shun AMT

Depreciation is a preference item for Alternative Minimum Tax (AMT). Adding this significant expense back to taxable income (in order to calculate AMT) effectively neutralizes the tax benefits of owning equipment in the first place.

With AMT, anything that boosts depreciation only worsens the problem.

Organizations that are near to (or already) paying AMT generally want to avoid creating more depreciation expense. Anything that boosts depreciation (such as bonus depreciation or a short recovery life) only worsens the problem. Using a tax lease can help minimize the creation of additional tax depreciation.

Alternatives to bonus depreciation

Organizations facing an NOL or AMT situation may consider a tax lease. Tax leases shift the tax ownership of equipment (and the asset's depreciation) from the equipment user to a Lessor. In this way, the organization gains access to needed equipment without harming its tax optimization strategy. Because the Lessor benefits from greater depreciation (including bonus depreciation) on its own tax return, it typically shifts some or all of that benefit to the client in the form of lower overall financing costs.

Those not familiar with tax lease financing find assurance in the amount of control an organization retains over the equipment and structure. With a lease (as opposed to a full-service rental), the organization selects the vendor, equipment brand and equipment deployment. Also, most tax leases include an option to purchase or return equipment, or to renew the lease at the end of the finance period. Tax leases can be structured as a capital or operating lease under FAS 13,[3] depending on structure specifics and the organization's financial objectives.

Opportunities

The extension of Bonus Depreciation through 2013 (and 2014, for some equipment) offers opportunities to healthcare enterprises. A clear strategy and proactive planning can help your organization fully optimize the benefits of the Bonus within the context of your larger financial goals.[4]

To learn more

Visit [website URL], call [phone] or email [contact], [title].

About the author

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[3] Financial Accounting Standards Board; www.fasb.org/pdf/fas13.pdf

[4] Consult your financial advisor before entering any equipment finance arrangement.

PERSPECTIVES IN BANKING:

Three Key IT Trends Lead Back to the Customer

ABSTRACT

As banks prepare for the future, they face the over-riding challenge of acquiring and retaining their most valuable of assets, customers. Successfully meeting this challenge requires a well-considered approach to Information Technology (IT). This article explores three IT trends in a new age of customer-centric banking. They include (1) increased recognition of customer value, (2) command of customer information, and (3) participation in the customer-rich environment of the Internet.

TREND ONE: INCREASED RECOGNITION OF CUSTOMER VALUE

"As technology access has expanded, the real control over financial relationships has shifted from the provider to the user." — Bank Administration Institute.

TO FORESEE THE FUTURE OF BANKING, WE NEED ONLY LOOK at today's banking customer, popularly, though inaccurately, portrayed as "fickle" or even "disloyal." In reality, the customer has become more discerning, better-informed, and increasingly empowered to choose from a wide variety of highly competitive financial services. And the best financial-service providers have responded — and will continue to thrive — by catering to the customer's requirements specifically.

Proactive, Customer-Centric Approach

A few months ago my sister received correspondence from her wireless-phone company. "We have reviewed your account activity," the personalized note read, "and believe you might benefit from the alternative plan described here." A side-by-side chart compared her current plan with a new one. She was dubious, but the "alternative plan" did indeed offer better features for her purposes, as well as cost savings of a few dollars a month. She not only signed on for the new plan, but became a proponent of the company. After all, how often does a phone company — or a bank, for that matter — contact you to offer better products and services that also save you money?

Of course, the company in question was being shrewd and proactive. In a competitive market, another wireless service would likely make the same or a better offer. From her perspective as a customer, however, these facts held little interest. Her wireless provider reached her first, demonstrated an understanding of her needs, presented some well-considered benefits, and won her over.

No Added Value, No Customer

In contrast, consider the recent experiences of my friend Jeff Walker at XYZ Bank. (Both names are fictitious, but the circumstances recounted here are factual.) Located in the midwest, XYZ is a commercial bank with 100 statewide branches and $4 billion in assets. Over the past few years, Jeff, a well-paid civil engineer, had accumulated about $60,000 in various accounts at XYZ. Like many affluent Americans, Jeff claimed no great knowledge of finance and money management and, until recently, simply entrusted such matters to his bank.

He realized, however, that most of his money at XYZ was in low-interest accounts. He knew there were ways of obtaining higher rates, but he lacked the time to investigate them. XYZ never offered such services to Jeff. Then a friend told Jeff of his experience with one of the new brokerage-banker

firms. It was like having a personal banker and financial advisor, the friend said, and the interest rates were higher than those Jeff earned at XYZ. Soon after, Jeff withdrew nearly all his funds from his bank, keeping only about $1,000 there in order to maintain a local checking account. The balance of the funds went to the brokerage-banker.

Could XYZ have prevented its loss? Probably. In fact, XYZ even offers money management services and interest rates comparable to those of the brokerage-banker. But the bank had lost touch with a customer. "In the ten years I banked at XYZ," Jeff says, "Their main communication with me was monthly statements."

TREND TWO: GETTING A GRIP ON CUSTOMER INFORMATION

"It is frustrating to see banks so under-realize their potential. They have all the pieces. If they can get them to work together, they would be able to compete." — Neil Bathon, Financial Research Corporation.

When XYZ failed to communicate effectively with a long-term, profitable customer, it ran and realized the unnecessary risk of losing him. In all likelihood, the central cause of the communications failure could be traced to a deficiency within the bank's information systems.

Database Integration A Top Priority

Most bank databases are organized on the basis of product, a troubling situation in an industry that faces an imperative transition to a customer-centric culture. "Most firms have yet to successfully integrate these databases so that they can move from a focus on the profitability of individual products to a focus on each customer's lifetime value to the firm."[1]

"...a focus on each customer's lifetime value to the firm."

In other words, relevant customer information exists within the bank, but the bank cannot access it. Small wonder that, in a recent survey conducted by the California-based Computer Sciences Corporation, more than 75 percent of financial-services IT executives cited "organizing/utilizing data" as their single most critical technology issue.[2]

Further, the price transparencies that pervade the financial-services sector today are best combated through differentiation of various products and services. At its core, differentiation reflects knowledge of the customer. It demonstrates that a bank knows, understands, and will act upon customer desires and requirements. Effective differentiation, therefore, can occur only after the successful integration and refocusing of a bank's databases.

IT Investments Higher, Sharper

The days of Y2K-related IT expenditures behind us, we see a marked shift in IT priorities. In light of the pressing need to reorganize, refocus, and refine customer information, bank IT investments, especially those concerned with customer relationship management (CRM) and strategic technologies, will rise.

- In 2007 retail and wholesale banking IT commitments totaled $26.9 billion. By 2012 that figure should rise to $82 billion.

[1] "Competing For Your Customers," Deloitte Consulting, www.dc.com, 2007.
[2] "IT Remodeling: Becoming Customer-Centric," *Bank Systems and Technology,* May 2007.

- In recent years, expenditures on strategic technologies such as branches, call centers, and online banking have averaged about 15 to 20 percent of the IT budget. This year, about 27 percent of the overall IT budget will be devoted to strategic technologies.

- Over the next five years, bank IT investments in retail delivery and customer information systems will rise more than four times faster than back-office IT expenditures.[3]

In addition, two IT adjuncts, automated text recognition systems and the application service provider, will also play key marketing roles in banking's future.

— ASP Assistance in the IT Arena

In efforts to keep pace with customer information and a growing demand for improved products and services, financial institutions (including Mellon Enterprise Cash Management, Chase Manhattan Mortgage Corp., and Providian Financial Corp., among others) now look to application service providers (ASPs) for IT assistance.

The ASP functions as a kind of electronic service bureau, delivering software solutions (for CRM or a variety of other services) via the Internet. Because using an ASP requires little or no capital outlay for hardware, software, or staffing, it is fast becoming a popular technology tool in small to mid-sized banks. Maryland-based OBA Federal Bank (assets $250 million), for example, uses an ASP for its E-banking services. As a result, the bank circumvented an initial investment of around $150,000 and today saves about $70,000 a year.[4]

— Paper Persists; Recognition Rises

Though much of the banking industry's future is geared toward electronic and online functionality, paper checks will persist as a favored method of payment. Each year Americans write about 65 billion checks worth around $75 trillion. Those numbers will likely decline, though only at a very gradual rate.

"...you can use your image archives to leverage a lot of business."

Even today, some banks have begun using software systems that can read a check's legal and courtesy amounts as well as its payee line. The acquisition of payee-line information represents a dramatic breakthrough in bank marketing resources, providing accurate, customer-specific data for use in CRM and cross-selling initiatives. As Richard Oliver, senior vice president and retail product manager at the Federal Reserve Bank of Atlanta, has observed, "A central image system store is something that smaller institutions are going to want. If you're really big, you can use your image archives to leverage a lot of business."[5]

Furthermore, hard-copy documents will still be required components of many financial transactions in the foreseeable future. Currently, for example, a mortgage applicant's supporting documentation for a loan package often consists of a dozen or more disparate paper forms, from 1040s to paycheck stubs. Recognition technologies similar to the check-based systems described above can also be used to acquire information from nearly any imaged form or document. Note also that, because the recognition process is automated, it greatly reduces the overhead associated with manual data entry and text conversion.

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[3] Datamonitor.

[4] "A Cautious Embrace," *Bank Systems and Technology,* September 2007.

[5] "Moving Money," *Bank Systems and Technology,* August 2007.

TREND THREE: GOING WHERE THE CUSTOMERS ARE

"...Information technologies have begun to alter significantly how we do business and create economic value, often in ways that were not foreseeable even a decade ago."[6] — Ben Bernanke, Chairman, Federal Reserve Board.

Information Technology enables banks to serve customers in ways that are at once personalized, profitable, and efficient. IT is about the quest for customers, but customers want more than just great service. In fact, they want more than just branch offices, phone banking, and ATMs. They want to go online, or wireless, or satellite TV. They want, it seems, whatever might be available, whatever some *other* bank may offer.

Seamless, multi-channel, multi-touchpoint delivery systems pose a serious problem for some banks that cannot afford investment in the required infrastructure. At a handful of banks now, however, a customer can contact a call center, transfer funds online, apply for a loan through a Palm Pilot, and check an account balance via a cell phone — all in the same day, all with the same bank. Some analysts insist that this kind of channel saturation will be the salvation of banks, while others are more restrained in their views. Nonetheless, nearly all acknowledge that Internet banking has emerged as a significant market force.

E-Banking: Facts, Figures, Forecasts

Overall, we can expect the base of online consumers, which numbered 100 million in 1999, to increase to 600 million by 2010. By 2012, more than 70 percent of large companies will embrace the Internet as a sales tool; Internet revenues, projected at $942 billion in the U.S. alone, will exceed $2.1 trillion worldwide.[7]

Given the Internet's past performance and growth, as well as the stunning projections for web proliferation, banks have been slow to jump on the E-bandwagon. That reticence, however, is fast changing to an urgent desire to participate. The recent TowerGroup report, "Internet Banking: The Bank's Perspective," notes that U.S. banks will likely invest $2.1 billion on E-banking technology in 2012, up from the current level of about $500 million; see Figure 1. The lion's share, about $1.2 billion, of the projected 2012 investment will go to channel management.

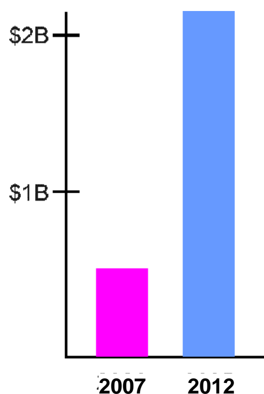

Figure 1. E-Banking Technology Investments

[6] "Structural change in the new economy," address to the National Governors' Association, July 11, 2007.

[7] Forrester Research, cited in *"The Unstoppable Economic Tidal Wave: How the Internet Continues to Shatter the World's Fundamental Business Paradigms,"* Deloitte Consulting, www.dc.com.

And where does U.S. E-banking stand today? The larger the bank, the greater its online presence; see Figure 2. A "presence," however, does not necessarily indicate functionality, that is, the capability to conduct transactions online.

Assets	Number of Banks	Online Presence
Less than $100M	5,912	5%
$100M to $500M	3,403	16%
$500M to $1B	418	34%
$1B to $3B	312	42%
$3B to 10B	132	52%
More than $10B	94	84%

Figure 2. Online Banking Presence (Source: FDIC, March 2007)

As shown in Figure 3, only 23 of America's top 100 banks offer transactional websites. Thirty-six of the top 100 do not have Internet sites, while the remaining 41 maintain websites that are merely informational.

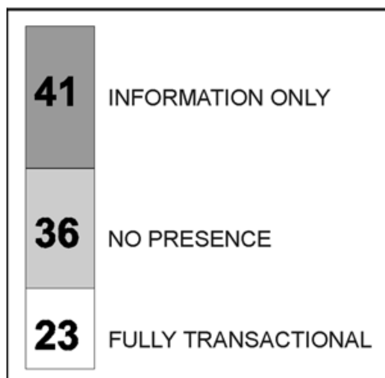

Figure 3. Online Status of the Top 100 U.S. Banks (September 2007)

Today about 1,100 U.S. banks, large and small, provide full-fledged, transactional banking online. Analysts anticipate the arrival of an additional 1,200 transactional online banks in just the next two years. By 2012, the number of such banks should increase to more than 3,000.[8]

And if you E-build it, will the E-customers come? Apparently. Gomez Advisors observes that about 11 million people use Internet banking today, and forecasts an increase to 48 million users by 2012. In a more conservative projection, IDC estimates that by 2011 U.S. retail banks will serve 40 million online customers and generate $820 million in online revenues.

[8] TowerGroup.

OBSERVATIONS AND CONCLUSIONS

"Businesses are facing changes more extensive, more far-reaching in their implications, and more fundamental in their transforming quality than anything since the modern industrial system was established. Increasingly, what distinguishes the winners from the losers is the ability to anticipate and influence these kinds of changes — to be masters, not victims, of change." — Rosabeth Moss Kanter, Harvard Business School.

Even if the customer is not always right, the customer is always most important.

Over the past decade, of course, banks have undergone more than their share of changes, including those engendered by consolidation and deregulation, both of which are beyond the scope of this article. Perhaps the most dramatic of changes, however, have arisen from rapid advances in technology. Today American banking stands at the threshold of a new, customer-centric era fueled by the capabilities of Information Technology.

The foremost banking challenge posed by this new age is cultural. Banks must move from a product-focused environment to a personalized business world where, even if the customer is not always right, the customer is always most important. The next challenge involves taking control of customer information and leveraging it in ways that benefit both the bank and the customer. Though not long ago the Internet was mostly a curiosity and haven for scientific research, it has now grown into dynamic marketplace ripe for financial-service opportunity. Banks that tap the omnipresent Internet resource will better serve not only their customers, but themselves.

American banks today seem especially well situated to meet the challenges of this new IT age. In 2007 earnings for U.S. commercial banks reached a record-high $71.1 billion, and economic growth has created an estimated $26 trillion of new household wealth. True, the technologies required to win and retain profitable customers are not cheap, but they are available, generally affordable, and they offer a tangible return on investment. Prudent use of Information Technologies will create the pathways, both physical and virtual, to mutually rewarding relationships with the all-important banking customer of the future.