Legacy Advisors Group

M & A UPDATE®

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Pending Legislation and Its Tax Planning Impact on Business

Bart A. Basi, CPA/Attorney at Law
The Center for Financial, Legal & Tax Planning, Inc.

Introduction

If you live in the U.S. you are well aware of the economic situation. According to The Beige Book, published by The Federal Reserve, nearly every sector of industry and agriculture and every geographical region of the country is experiencing an economy that is essentially stuck in neutral. While some indicators suggest the recession is over from a Gross Domestic Product standpoint, nearly every other indicator including employment, spending, job security, and the consumer confidence index all suggest the populace is not in prime condition.

America's leaders are at work trying to draft policies that will facilitate our way out of the current situation. There are several issues on the table that are important to us all and will be addressed in the coming months and years. Among the more important topics and well known legislation currently being considered include the estate tax, the income tax, and healthcare legislation. The following is an update as to where these topics are and how they will be addressed.

Estate Tax

Currently, the estate tax has been repealed; meaning that if a person passes away by December 31, 2010 at 11:59 p.m., their estate, no matter how large, will not be subject to a tax due the government. Under the current law, the estate tax is to be reinstated January 1, 2011 with an exemption of $1,000,000. While the estate tax was intended to apply to wealthy individuals, the return of the estate tax would affect many more middle class individuals with homes and retirement accounts. It is not the intention of Congress or the President for the middle class to have such a tax burden.

A lot of discussion has taken place in Congress. It is likely and probable that the estate tax exemption of $3.5 million will be reinstated for 2011 and subsequent years. Congress has already taken some action on this matter and this scenario looks likely. However, we are strongly suggesting that you review any trust documents, especially marital and bypass trusts if you have them, as well as your overall estate plan to be sure

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Mike Ertel is a Certified M & A Advisor and a Principal Broker with Legacy Advisors Group, a full-service M & A Advisory firm with an office in Tampa, Florida specializing in representing sellers and buyers of small- to mid-sized companies. Prior to joining Legacy Advisors Group, Mike's business career spanned 30+ years with Fortune 500 and Fortune 1000 Companies, with senior management roles in Marketing, Operations and Logistics. Mike also served as President, COO of a mid-sized Manufacturing company headquartered in Tampa. Mike also holds a BS in Electrical Engineering and an MS in Industrial Administration, both from Purdue.

A CASE STUDY

The Tax Court held that a settlement payment received by an S corporation for a trade secret misappropriation lawsuit was taxable as ordinary income. In the case, the corporation entered into a settlement agreement with another company. The S corporation listed the settlement amount as capital gain. However, the IRS denied this claim, stating that the settlement amount was ordinary income. While the corporation argued that the damaged trade secret was a capital asset, the Court held that the damages represented lost profits which are taxable as ordinary income.

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it is current and will achieve the goals you originally intended.

Income Tax

There is plenty to be said about other areas of the tax code. As of the start of this year, the Section 179 deduction for business equipment purchases has been lowered from $250,000 to $134,000. Additionally bonus depreciation has expired as of January 1, 2010. The 15% capital gains and dividend rates are set to expire at the end of 2010. The consensus is that bonus depreciation may not be reenacted; however Section 179 deduction amounts are expected to be raised to $250,000. As far as the capital gains and dividend rates are concerned, it is expected that the capital gains tax rate will be lower than the dividend rate, which is expected to go up a considerable amount. Certain tax planning scenarios have come about as a result of the "sunset provisions" of many income tax laws. You are advised to address all of the issues with a competent tax planning advisor, not necessarily the individual who files your tax returns.

Healthcare

The healthcare debate is better known than the tax situation. From a planning standpoint, it is our advice that you review the benefits package for your employees. It is likely that you will want to at least be in a position where you can easily modify your benefits package as needed to provide the necessary health benefits to your employees, while not incurring large financial losses if and when a healthcare mandate becomes law.

Other Economic Legislation

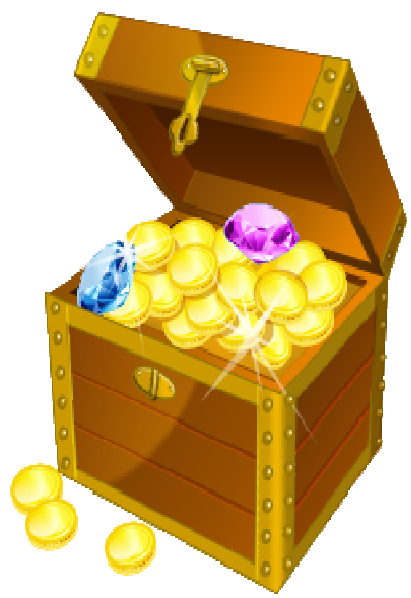
There are many laws on the table concerning tax policies to facilitate business and better the employment situation. Such areas include "green jobs" and certain other tax credits. From a tax planning standpoint, it is best to keep all tax credits and deductions in mind as they are enacted into our law, so you can utilize them when the time comes. These credits include fuel efficient vehicle deductions and energy tax credits.

Conclusion

As individuals and business owners, we can all benefit from the tax laws passed in Washington and our state governments. While the legislative process continues to finely tune our tax laws, we must plan for the future and not wait. It is our advice that you have your estate plan, employee benefits plan, and your income tax strategies reviewed at once to reflect the current laws. The Center's professionals routinely advise clients on these matters and are available to properly address your concerns.

A CASE STUDY CONTINUED:

Editor's Comment: The argument used by the taxpayer in this case was that because they claimed damage to a capital asset in their lawsuit, the settlement amount represented that damage. As a result, the settlement amount represented capital gain. While this argument seems logical, the Tax Court saw the amount received as lost profits due to the damage to the capital asset, making it ordinary income. As a result, the taxpayer incurred a higher tax liability.



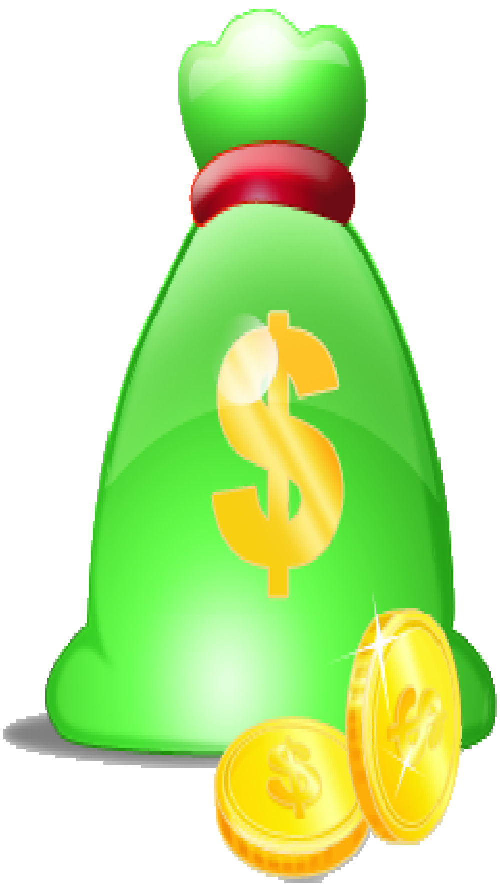
Dr. Bart A. Basi is an attorney, CPA, and the Senior Advisor of The Center for Financial, Legal & Tax Planning, Inc, a full service company specializing in financial, legal & tax matters. Basi is a nationally recognized author, lecturer, and advisor on how to structure deals to minimize taxes. Tax structure makes the difference between getting the deal done and watching the deal fall apart. Many of you may be familiar with Basi and the topics he covers in the Financial, Legal & Tax Advisory which may be read in various industry-specific trade publications.

Legacy Advisors Group
1101 Channelside Drive, Suite 290
Tampa, FL 33602-3611

The Center for Financial, Legal & Tax Planning, Inc.
4501 W. DeYoung St., Suite 200
Marion, Illinois 62959

Points of Interest

- **. . . nearly every other indicator including employment, spending, job security, and the consumer confidence index all suggest the populace is not in prime condition.**
- **It is likely and probable that the estate tax exemption of $3.5 million will be reinstated for 2011 and subsequent years.**
- **It is our advice that you have your estate plan, employee benefits plan, and your income tax strategies reviewed at once to reflect the current laws.**



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WHAT DO THE VARIOUS PROFESSIONAL DESGINATIONS MEAN?

Mike Ertel, CBI/ M&AMI/ CM&AA

Many professional M&A advisors display one or more professional designations behind their name, or in their signature block, in addition to the abbreviations for the college degrees they may have earned. While some college degrees are familiar to many business owners and potential business buyers, they have no idea what most professional designations mean.

COLLEGE DEGREES: The common college degrees are: Bachelor of Arts (BA), Bachelor of Science (BS), Master of Arts (MA), Master of Science (MS), and Doctor of Philosophy (PhD). These are frequently followed by one of more letters to indicate the specific field of study. In my own case, I hold a BSEE, which is a Bachelor of Science in Electrical Engineering.

Other degrees frequently held by professional M&A advisors include a BA in Business, or Accounting, a Masters in Business Administration (MBA). One of my associates, Marty Adams, has a Juris Doctor, which is the first professional degree in Law. Another colleague, Mark Fitzgerald, holds a Master of Science in Entrepreneurship (MSE), which is on a par with an MBA, with a more quantitative and entrepreneurial focus. In my own case again, I hold a Master of Science in Industrial Administration, which is akin to an MBA with a more quantitative and technical focus.

PROFESSIONAL DESIGNATIONS/ CREDENTIALS: There are several professional development programs which are specifically geared to training someone to become a professional business intermediary. The more common ones are Certified Business Intermediary (CBI), Merger & Acquisition Master Intermediary (M&AMI), and Certified Merger & Acquisition Advisor (CM&AA). Each of these requires a minimum of one to three weeks of intensive classroom education, followed by passing a comprehensive, written examination lasting three to four hours. There are also continuing education requirement to maintain any of these credentials.

There are many more professional designations for those who specialize in performing business and/or equipment appraisals. These include: Accredited Senior Appraiser (ASA), Accredited Valuation Analyst (AVA), Certified Business Appraiser (CBA), Certified Senior Business Analyst (CSBA), Certified Valuation Analyst (CVA), Certified Machinery & Equipment Appraiser (CMEA), Accredited in Business Appraisal Review (ABAR), Business Valuator Accredited in Litigation (BVAL), and Master Certified Business Appraiser (MCBA). Many business appraisers also hold a Certified Public Accountant (CPA) designation. Each of these has its own education, exam, and continuing education requirements. In addition, each granting authority has its own standards of professional practice, which holders must abide by.

BOTTOM LINE: There's a great diversity of academic and professional training available for business intermediaries and M&A advisors, so why not work with someone who's invested in their own professional development to assist you with one of the largest financial transactions of your working life?

If you know of a business owner who's thinking of selling or buying a business and who might benefit from a free, confidential, consultation with us, have them contact me at mertel@legacyadvisorsgroup.com

Legacy Advisors Group
813.299.7862 Direct
mikeertel@legacyadvisorsgroup.com

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Legacy Advisors Group
1101 Channelside Drive, Suite 290
Tampa, FL 33602-3611
Phone: 888-864-6610
Fax: 866-353-0382

The Center for Financial, Legal & Tax Planning, Inc.
4501 W. DeYoung St., Suite 200
Marion, Illinois 62959
Phone: 618-997-3436
Fax: 618-997-8370
Satellite Office:
Longboat Key, FL 34228
Phone and Fax: 941-383-3338

We're on the Web!

www.taxplanning.com
www.legacyadvisorsgroup.com

Frequently Asked Questions…

Q: I am interested in contributing money to my Individual Retirement Account for 2009. Can I still contribute money for the 2009 tax year and if so, when do I have to do this?

A: Taxpayers have until April 15, 2010 to make 2009's IRA contribution. Additionally, if one chooses to file their tax return before the contributions are actually made to the IRA account, one can do that as well.

Q: I want to establish a phantom stock plan for the benefit of my employees. What does this involve and how can I start it?

A: A phantom stock plan is a compensation system that rewards an employee's performance based on the overall performance and increase in value of the company. Since phantom stock is not comprised of physical shares of the company, phantom stockholders do not necessarily hold an equitable interest or voting interest in the company. The best way to start a phantom stock plan is to speak to a knowledgeable attorney and have him or her discuss your needs and act from that point preparing specific documents with specific language.

Q: I have recently had my business valued. The value between what I believe the value should be and what is calculated are completely different. Why is this?

A: There could be any number of reasons for this dilemma. Valuations are based upon assumptions, figures provided, and calculations based upon them. The numbers, assumptions, and calculations may not necessarily reflect the value of the business to an owner. There are methods and procedures available to improve the value of a business to a willing buyer. It is with these improvements, a business' value can be augmented.

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