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Congress Loves Race Horses!

Roman A. Basi, MBA/Attorney at Law
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Not to rail on Congress, but do you own a race horse? Of course not! How about a NASCAR track? Nope. A manufacturing facility in Puerto Rico? No such luck there either. On December 15th, 2015 Congress performed their perennial rescue of the misfit laws! While some of the tax extenders may be for very specific interests (and even comical in some respects), a lot of the extensions are useful to those in business. In addition to that, some of the extensions have been made permanent, which is excellent work coming from Congress!

What Could Have Happened?

Without the extenders, dozens of laws were set to expire 12:00am New Year's Day or not exist at all for the year 2015. Not just tax laws, but an entire basket of laws ranging from the exploration of Mars, to agriculture, defense, homeland security, and even military and veteran's affairs would and could have been affected.

Especially concerning for most business owners were the 52 tax laws and deductions that expired or missed their existence entirely as of January 1, 2016. Two of the most utilized deductions that would not have been allowed include the enhanced section 179 deduction and bonus depreciation. There were also individual level tax laws that were set to expire as well or not exist at all for 2015. For example, the itemized deduction for state and local taxes was set to disappear and cancellation of debt related to primary mortgages was also set to be lost.

What has been Extended?

The **enhanced section 179** was extended to the tax year 2015 and at a level of \$500,000, with a maximum investment limit of \$2,000,000 before the phase out begins. Once the phase out begins, it phases the deduction out dollar for dollar to the amount of \$2,500,000 in investments. This amount will be indexed for inflation in the future.

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A CASE STUDY

Bargain Sale to Charity

The Tax Court has ruled that a bargain sale to a charity qualified for a charitable deduction. The taxpayer held the intent that a senior center be built out of the property. He sold it to the buyer for \$2M. The property was valued at \$4.1M. The IRS disagreed with 1) the intent (saying it was not present) and 2) the valuation of the property (being way too high).

The Tax Court ruled that there was:

- 1) Intent based on all the preparation and research. The research and preparation took place over the course of years. Professionals were employed and counsel given.
- 2) The appraised value was about 3.6M. The appraiser did its work and thoroughly established the value with careful considerations being made.

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Exclusion of 100% of the Gain on Small Business Stock has also been extended. Under this provision, those selling stock in an appreciated small businesses, enjoy the benefit of being 100% gain free upon the sale of the stock. Qualifying Small Businesses are those starting with under \$50,000,000 in gross assets and the stock must be held for 5 years or longer.

The **Built in Gains** recognition period for S Corporations has been set for 2015 at 5 years. This applies to C corporations that convert to S Corporations. In the past, those that converted were liable for taxes at the same rates that would have been paid had they been a C Corporation for 10 years. This extended provision cuts this detriment to 5 years.

Permanency

In the past, business people and individuals alike had to engage in this will-they-or-won't-they kind of analysis only to hurry the issues along in the last weeks of the year. This year, permanency has been added. Specifically Section 179 is now permanent; however, the amounts are indexed to inflation adjustments.

The **Research and Development Credit** also hurt from this wait-and-see system of tax law. With Section 179 and bonus depreciation, the solution to a lazy tax law is simply a quick purchase of equipment. The problem with the R&D credit not being permanent was that research and development takes time. Not allowing medical, technical, and other research and development firms to have the certainty of a tax credit has frightened those firms into not funding the projects as they should have. The credit is now made permanent.

Conclusion

I'm sure many owners of race horses were happy to see the accelerated write-off of their horses. As a business person and individual taxpayer, I am happy to see this extension law passed as well. If you think you will be impacted by these tax extenders and would like details, there is a plethora of information online. As the name The Center for Financial, Legal & Tax Planning implies, we do a lot in the way of tax planning. We also do valuations and business succession for business owners and individuals as well. If you would like to have your business valued or succession plan made, give us a call at 618 997 3436.

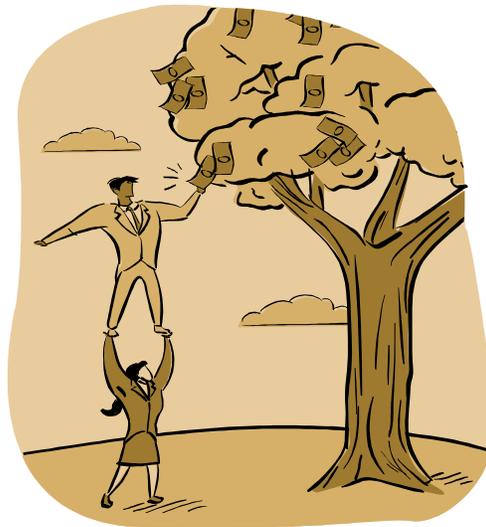


About the author:

Roman A. Basi, President of The Center, is an Attorney, Real Estate Broker, and Title Insurance Agent. Roman speaks and advises The Center's clientele on such matters as Business Law, Succession, Estate & Tax Planning and Real Estate.

Points of Interest

- On December 15th, 2015 Congress performed their perennial rescue of the misfit laws!
- I'm sure many owners of race horses were happy to see the accelerated write-off of their horses.
- Section 179 is now permanent; however, the amounts are indexed to inflation adjustments.



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A CASE STUDY CONTINUED:

Editor's Comments:

The rule here is nothing new. At the Center we have put together various charitable/part-sale transactions and have been successful. What is important is to have an appraisal done by a reputable firm that does excellent work. Also create evidence via written instruments to make it abundantly clear your intent was to in part donate the parcel.



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Benefits of Analyzing and Recasting/Restructuring Your Financial Statements

Working another client recently I was struck once again by the importance of analyzing and recasting - and possibly even restructuring - your company's financial statements as the first step in getting your business ready for sale.

Like almost all privately held companies, this client's financial statements had been prepared with the goal of minimizing taxes, rather than maximizing market value.

Over a period of years, the business had been expensing and/or depreciating all of its capital equipment purchases to the maximum extent allowable under the tax code, and expensing all of its research and engineering activities. As a result, the business appeared to be marginally profitable - and in some years actually showed a loss - and as a result paid very little in taxes.

However, when it came time to sell the business, a potential buyer looking at the business' own books and records and tax returns would have a difficult time discerning the intrinsic value of this business. The net book value of its equipment was shown at a fraction of its market value, and its annual income appeared to be very modest compared to its sales volume.

By analyzing and recasting - and in this case - restructuring its financial statements to better reflect the company's true value we were able to:

- Discover that the company had failed to take advantage of significant tax credits for its research and engineering expenses. By working with their tax accountant to file amended returns for the past few years, this client was able to generate additional tax credits totaling ~\$100,000.
- Document that the company was substantially more profitability over the last several years, and therefore commanded a substantially higher market value.
- Document the significant investment the company had made in developing several new products whose sales were just beginning to take off, creating additional streams of income and cash flow for the buyer, and
- Document the current market value of its plant and equipment

...all of which contributed to a much higher market value for the company.

If you know of someone who's thinking of selling or buying a business and who might benefit from a free, confidential, consultation, have them contact me directly at 813.299.7862, or mertel@lmaallc.com

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Frequently Asked Questions...



Q: I need a loan. Can a loan be taken from an IRA?

A: Loans are not permitted from IRAs or from IRA-based plans such as SEPs, SARSEPs and SIMPLE IRA plans. Loans are only possible from qualified plans that satisfy the requirements of 401(a) and from annuity plans that satisfy the requirements. Instead I would recommend getting a loan from a bank as opposed to doing this, because: (next question)

Q: What happens if a loan is taken from an IRA?

A: If the owner of an IRA borrows from the IRA, the IRA is no longer an IRA, and the value of the entire IRA is included in the owner's income.

Q: If I have a qualifying plan and take a loan and default, then what?

A: A loan that is in default is generally treated as a taxable distribution from the plan of the entire outstanding balance of the loan (a "deemed distribution").

It is usually always best NOT to borrow from a retirement fund. If you have employees thinking of doing so, be sure to advise them to talk to a tax professional first

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