2015 | ISSUE 09

CONTENTS

Lower your IRS tax when selling your business.

Most private business owners sell their companies to outside parties by selling the company assets, and may pay high tax rates on the sale. The seller, in these arrangements, is required to allocate a portion of the assets subject to IRS income tax rates that are as high as 43.4%. If your company has highly valued assets, your tax rate on the sale of these assets will be high. You may benefit from an IRS approved rule that lowers your tax bill.

Here's how it works: the seller structures the transaction as a sale of stock, selling the company's stock rather than selling the company's assets. There is a special IRS approved election that makes this possible.

The tax impact is that this IRS approved company stock sale is taxed at 23.8%. The IRS approved sale has requirements that must be met to qualify. This tax structure benefits both the seller and the buyer.

The main tax benefit to the seller is that he treats the transaction as a sale of the company's stock which is at the capital gains rate, currently 20% plus an additional 3.8% tax, if the seller's tax bracket is above $200,000 for single taxpayers and $250,000 for married filing jointly.

The main tax benefit to the buyer is that the transaction is treated as purchase of the seller's assets, thus the buyer depreciates the acquired assets annually. The depreciation lowers the taxable income over time. In the sale of stock without this IRS election, the buyer does not have the deprecation / tax benefit.

The IRS section is known as a 338(h) election. Some of the requirements for this election include:

1) In general, the purchaser and seller must be corporations. The purchasing corporation must purchase at least 80% of the stock of the target corporation. The first date on which the purchaser has acquired 80% of the seller's stock is the "acquisition date."
2) Purchaser at the acquisition date must make an election to have section 338 apply within 8 ½ months after the month in which the acquisition date occurs.

3) The purchaser must be a new corporation (New Co.) that buys the selling corporation on the acquisition date. The purchaser that creates the New Co. holds the stock of the old, selling corporation at the acquisition date. The purchaser is the sole owner of the stock in New Co.
4) The selling price must be equal to the fair market value of the seller's assets and liabilities.
5) There are additional risks to the purchaser in this arrangement. The New Co. is responsible for the seller corporation's liabilities. Extensive due diligence is essential for the purchaser.

These requirements must be adhered to strictly to qualify for the IRS approved transaction. In order to consider this election, seek advice from your tax advisor regarding your facts and circumstances. Each taxpayer's situation should be adequately reviewed before making an important decision on how to best plan for the tax consequences in the sale of your business.

Diamonds in the rough - employee ideas.

Too many owners and managers simply dismiss out of hand ideas put forth by their employees without proper consideration. That can be a costly mistake. Your employees are on the firm's front lines providing customer service. They see the strengths and weaknesses of your customer interaction as well as certain operations within your business.

When an employee comes to you with a suggestion, what is your usual reaction? If it's along the lines of "*That's never going to work*", "*That's not your problem*" or "*We don't have time to think about that*" – or any equally negative response, then you could be missing out on a great opportunity to grow your business and increase its value.

Because employees are the people closest to the action, be it on the production line, in the admin office or on the floor dealing with customers, they see and hear a lot and are often led to think about, or even invent for themselves, better ways of getting things done. Better ways that can improve productivity, morale, process efficiency and ultimately, profits. It is important to openly encourage employees to come forward with their suggestions and to make them feel that they contribute to the decision making process.

One caveat as with everything in business, the better the planning you put into an initiative the more value you get out of it. A poorly conceived, hastily launched, undefined employee suggestion program can backfire and achieve just the opposite of encouraging ideas – it can turn people off by creating bad feeling and making them more cynical.

There are a number of channels you can create to receive employee suggestions. Some will suit one business more than another; some businesses may find they can use more than one of them. Most basic is the suggestion box. These days a suggestion box needn't be a physical thing, it can be an email address employees use to email in their suggestions. The brainstorming session is a more formal approach and involves a greater commitment of time and money.

Tips for an effective employee suggestion system

1. Set clear goals and guidelines for the suggestion program. If the program is publicized as being about ideas that will achieve cost savings or about achieving a better level of workplace safety then you have immediately screened for what you want to hear about. If the program is totally open to any suggestion then point that out.
2. Deal with suggestions quickly. Delay a decision more than a week and people will see the suggestion box as a black hole.
3. Acknowledge receipt of valid suggestions. Never reply to obscene or abusive suggestions. Your best response to that sort of negativity is to not indulge the sender with a reply.
4. Let the contributor know the result. If their idea got the thumbs down explain in detail why you can’t use it. If the idea is worth implementing, tell the whole team so they can see the process at work.
5. Make the decision process transparent and fair – if the suggestion reviewer is the boss alone or just the top managers, rejection may be taken as just another instance of management negativism
6. If the suggestion gets the thumbs up carry through the implementation. Nothing builds trust and credibility faster than keeping a commitment.
7. Tie implementation into a reward program but don’t reward for suggesting alone, reward only acceptable suggestions. Otherwise you’ll spend a lot of money on rewarding ‘get a new coffee making machine’ type suggestions. The program is about quality suggestions. Your rewards don’t have to be of great monetary value. Common rewards include tickets to events, gift vouchers and restaurant meals.

Employee suggestions that have saved their company significant amounts of money run from the ‘eureka’ moment to the banal – but they all save money. It was an employee’s suggestion to build an elevator on the outside of the El Cortez Hotel in San Diego rather than, as the engineers had suggested, cut a hole through each of the floors internally. That saved engineering fees, cleanup costs and loss of income from having to close for the duration. Smart managers understand the potential of employees to come up with good ideas and encourage them to do so. You can too. But do it properly. People are easily discouraged and the process can become the butt of jokes if not taken seriously by management.

Best practices for budgeting.

There are six elements of effective budgeting. It is an important management tool. Being a projection of your income against your expenses you can check the budget at any time to see how well or how poorly your business is doing. The value of a budget is in direct proportion to the accuracy of the figures you use to create it. Here are some precautions to take to keep your budget figures accurate.

Use realistic projections

Since a budget is based on projections there's always an element of uncertainty involved in estimating inputs. It pays to be conservative regarding things such as sales forecasts. If they turn out to be better than estimated, that's great and provides the opportunity to distribute the extra around to advantage. But if they are worse than expected it means rethinking all your plans to match the budget shortfall. If your business provides a product or service for which the demand varies by season (retail takings over a holiday season, pool maintenance between seasons and so on), then factor that into your budget.

Don't underestimate costs

Gasoline, travel, raw materials, rent – all costs increase over time. A projection of costs at current year value will result in budget blowouts. It's wiser to make a best estimate and then increase it a little. If the actual costs do end up coming in under projection you will have provided a little bit of 'fat' in the budget to cover the odd unanticipated contingency. You might even add a 'miscellaneous' line item to the budget to handle those unknowns.

Question every expense

Preparing a budget provides the perfect opportunity to consider what value for money you are getting from the costs you are incurring. Is it time to change the gasoline powered work vehicle to a hybrid? Look at raw material substitutes? Move to a VoIP phone service? Also look for any expense items that could be eliminated. A penny saved is a penny earned!

Factor in cash flow

Incorrectly projecting cash flow will turn the best budget into a fiasco. In virtually every transaction there is a lag time between the finalization of the deal and actual cash collection. This time lag has to be built in when preparing a budget – you may expect to sell goods to a certain value in Month X but that doesn't mean the value of those sales will be in your bank account in Month X. This doesn't present a problem if the budget allows for it. When it's not factored in you can run into serious cash flow problems through spending money you don't yet have.

Allow for your tax liability

Don't forget your likely obligations to the taxation department. Sales income will ultimately be depleted by sales tax, various other state and federal taxes and employee withholdings. Fail to account for these and you run the risk of budgeting for future projects that you aren't going to be able to afford.

Keep the figures current

Budget preparation isn't a once a year operation. Things change – the price of gasoline soars, sales are a lot better than expected. Budget lines need to be revised to reflect these events. The point of budgeting is to be able to compare actual amounts against projections to see how the business is going. If the actual amounts aren't closely estimated amounts, you'll be making decisions based on false assumptions.

It's easy to let the budget become just another document gathering dust on the shelf. It will take self-discipline to plug in the new figures each month, consider how actual amounts are tracking against projections, and determine next steps. If you don't do it, you've not only wasted the time and effort you put into creating the budget, you open the path to fiscal irresponsibility and wasted opportunities as off-the-cuff purchase decisions send expenses out of control while unexpected income sits in a bank account when it could be put to use to improve operations.

Regular Pieces

How To Make The Most Of Your Newsletter

Be sure to read each article with the mindset 'How could this apply to our business.' Thinking of it that way will guarantee that you get value. Better yet, take notes as you read and commit to having the ideas implemented by the time the next edition arrives. Also, make copies for each team member. To really make sure something positive happens, work with your business development specialist to talk your team through the ideas and how to set a schedule for getting them implemented. We're here to help you get started.

An Important Message

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