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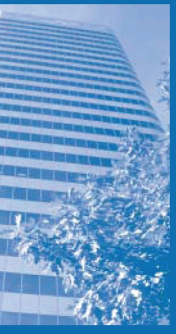

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Selling Your Business in 2010 When Federal Tax Rates Are Still Low

By: Phil W. Jaeger, Esquire and Ronald A. Feuerstein, Esquire

We are writing to provide a time-sensitive alert on current long-term capital gains tax rates and the higher rates that are likely to be enacted by Congress for January 1, 2011 and beyond.

If you are thinking about selling your business, you should consider selling your business in 2010 when Federal long-term capital gains tax rates are still low. After 2010, the Federal long-term capital gains tax rates on the sale of your business will probably rise from the current Federal rate of 15% to at least 20% and possibly higher.

During 2010, most owners who sell their business will pay the top Federal long-term capital gains tax rate of 15%. Under the current Federal income tax law, the top 15% long-term capital gains rate is scheduled to expire on December 31, 2010 and revert to its former pre-May 6, 2003 level of 20%. Given Congress' need to raise revenues to pay for increased spending to support the economy, national security and deficit reduction, the question is: Will the top Federal long-term capital gains tax rate rise only to 20% or will Congress raise the long-term capital gains tax rate higher?

During the past 35 years, the top Federal tax rate on long-term capital gains has ranged from 35% in 1976 to 15% in 2003. The top Federal rate on long-term capital gains was reduced in 1978 from 35% to 28% and in 1981 was reduced to 20%. In 1987, the top Federal capital gains rate was again raised to 28%. Not until ten years later, in 1997, was the Federal long-term capital gains rate reduced again to 20%. The lowest (and current) rate of 15% became effective in 2003.

What will this pending change in the Federal tax law mean when you sell your business? If you sell before December 31, 2010, for every $1,000,000 in gain on the sale of your business, you will pay $150,000 (i.e. 15%) in long-term capital gains tax. If you sell after December 31, 2010, for every $1,000,000 in gain on the sale of your business, you will probably pay at least $200,000 (i.e. 20%) in long-term capital gains taxes, and would pay $250,000 (i.e. 25%) if the long-term capital gains tax rate increases to 25%.

Consider, if you sell your business for $20,000,000 above your basis before December 31, 2010, you will pay long-term capital gains taxes of $3,000,000 (i.e., 15% of $20,000,000) for net after-Federal income tax proceeds of $17,000,000 ($20,000,000 less $3,000,000). If you sell your business for $20,000,000 above your basis after December 31, 2010, and the tax rate increases to 20% you will pay long-term capital gain taxes of $4,000,000 (i.e. 20% of $20,000,000) resulting in net after-Federal tax proceeds of $16,000,000 ($20,000,000 less $4,000,000). Therefore, by selling your business for $20,000,000 above your basis before December 31, 2010, you will probably save $1,000,000 in additional Federal income taxes (at a 15% rate vs. 20% tax rate on long-term capital gains) and you may save

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$2,000,000 in additional Federal income taxes if the tax rate increases to 25%. If you are thinking about selling your business, you will probably do better by selling in 2010.

If you would like to discuss the above article please contact our M&A lawyer, Phil W. Jaeger, or our tax lawyer, Ronald A. Feuerstein:

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SEXUAL DISCRIMINATION IN THE WORKPLACE - HOSTILE ENVIRONMENT

By: James V. Irving, Esquire

The Fourth Circuit Court of Appeals has overturned the dismissal of a hostile work environment claim, reinstating the complaint brought by the EEOC on behalf of a female physician who was employed by a family medical practice in Hickory North Carolina. The case is EEOC vs. Fairbanks Medical Clinic P.A., decided on June 18, 2010.

Dr. Deborah Waechter claimed that Dr. John Kessel, the sole owner of Fairbrook Medical Clinic, had created a hostile work environment through a pattern of offensive, sexually-related conduct.

Dr. Waechter accepted a position at the Clinic after completing her residency in 2002. According to Dr. Waechter, Dr. Kessel began making sexually-explicit comments to and in the presence of Dr. Waecher soon after she joined the practice. The offensive comments usually related to the male or female anatomy and often employed crude or graphic terms to describe male and female body parts. These comments sometimes left Dr. Waechter "speechless" and "uncomfortable." On other occasions, according to Dr. Waechter, Dr. Kessel made unwelcome disclosures about his own sex life, commented on Dr. Waechter's breasts, showed her revealing photographs and implicitly suggested that they engage in sexual relations. In February of 2006, after she had found a new position, Dr. Waechter tendered her resignation. In June of 2006, she filed a complaint with the EEOC.

The District Court dismissed the Complaint, finding that Dr. Waechter had failed to satisfy the four prong standard necessary to support a hostile environment claim. In order to sustain such a claim, there must be proof that the conduct was unwelcome; that it was based on sex; that the conduct severely or pervasively altered the conditions of employment and created an abusive work environment; and that the conduct was imputable to the employer. The District Court ruled that Dr. Kessel's conduct was neither severe nor specific enough to meet this test because his conduct was not particularly frequent, that it mostly involved crude jokes that did not run afoul of Title VII, that Dr. Waecher did not miss work or feel severe psychological stress as a result of the conduct, and because Dr. Kessel's conduct did not include inappropriate touching or physical threats.

The Fourth Circuit disagreed.

In the District Court, Dr. Kessel argued that his comments weren't "based on sex" because he habitually made crude and vulgar comments to men and women alike, however the Fourth Circuit concluded that his reputation as a "shock jock" did not overcome the impression that the comments were sex-related. Nor was the appellate court persuaded by Kessel's argument that in a medical profession, tension breaking comments about the human body were to be expected and that the environment at the Clinic could not be judged as objectively hostile considering all the circumstances.

The examples quoted by the Court, and assumed to be true for the purposes of the Fourth Circuit's review, paint a picture of a vulgar, locker room scene characterized by sexually-specific and innuendo-laden comments. It also presents Dr. Kessel as a person who thought his comments were essentially harmless and certainly within the realm of business as usual in a small medical practice. Now a jury will consider Dr. Kessel's arguments. At a minimum, the revelations are highly embarrassing to this physician. He also now faces the possibility of a significant damages awarded against him.

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Even the well-meaning businessman must remember that the office is not a playground, and that comments of a sexual nature may well be perceived as offensive. If they persist, the existence of the business could be at risk. Wise business owners adopt and enforce a code of office conduct that prohibits and penalizes sexually-offensive conduct.

Jim Irving can be reached at (703) 525-4000, extension 280 or by email at jirving@beankinney.com.

Recent Tax Developments

By: Ronald A. Feuerstein, Esquire

The following is a summary of some of the most important tax developments that have occurred in the past three months that may affect you, your business, your family, your investments and your livelihood. Please call us for more information about any of these matters and what steps you should implement to take advantage of favorable rules and to minimize the impact of those that are unfavorable.

Deadline extended for closing home purchase to qualify for homebuyer credit. Relief has been provided to taxpayers who could not meet a key June 30, 2010, closing date for qualifying for the homebuyer credit. In general, both the regular first-time homebuyer credit of $8,000 and the reduced credit of $6,500 for long-term residents expired for homes purchased after April 30, 2010. However, if a written binding contract to purchase a principal residence was entered into before May 1, 2010, the credit could be claimed if the purchase closed before July 1, 2010. Under the relief measure, if a written binding contract to purchase a principal residence was entered into before May 1, 2010, the credit may be claimed if the purchase is closed before October 1, 2010. This extension allows homebuyers who signed a contract no later than the April 30, 2010 deadline to complete their closing by September 30, 2010.

Guidance addresses tax breaks for hiring new employees. Employers are exempted from paying the employer 6.2% share of Social Security (i.e., OASDI) employment taxes on wages paid in 2010 to newly hired qualified individuals. These are workers who: (1) begin employment with the employer after February 3, 2010 and before January 1, 2011, (2) certify by signed affidavit, under penalties of perjury, that they have not been employed for more than 40 hours during the 60-day period ending on the date the individual begins employment with the qualified employer; (3) do not replace other employees of the employer (unless those employees left voluntarily or for cause) and (4) are not related to the employer under special definitions. The payroll tax relief applies only for wages paid from March 19, 2010 through December 31, 2010.

Employers may qualify for up to a $1,000 tax credit for retaining qualified individuals. The workers must be employed by the employer for a period of not less than 52 consecutive weeks and their wages for such employment during the last 26 weeks of the period must equal at least 80% of the wages for the first 26 weeks of the period.

The IRS has issued guidance on these tax breaks in the form of frequently asked questions. These FAQs provide valuable information on subjects such as the scope of the exemption, how it interacts with other tax breaks and when an employer must receive the employee's certification of former unemployment status. For example, the IRS explains that the exemption and credit can be claimed for a new employee replacing a downsized employee.

Detailed guidance released on new small business health care credit. The IRS has issued detailed guidance on the small employer health insurance credit created by the recently enacted health reform legislation. Under the new law, effective for tax years beginning after December 31, 2009, an eligible small employer ("ESE") may claim a tax credit for nonelective contributions to purchase health insurance for its employees. An ESE is an employer with no more than 25 full-time equivalent employees ("FTEs") employed during its tax year, and whose employees have annual full-time equivalent wages that average no more than $50,000. However, the full credit is available only to an employer with 10 or fewer FTEs and whose employees have average annual full-time equivalent wages from the employer of not more than $25,000. The new guidance adopts a liberal approach to the new law's requirements, including three alternative methods for figuring total hours of service (important for determining how many FTEs an employer has), and also explains how small employers claim the credit if their state provides a credit or subsidy for employee health coverage. The IRS has released a state-by-state table of average health insurance premiums for the small group market for the 2010 tax year. The table is needed to calculate the credit for this year.

Guidance issued on new under age 27 rule for health coverage of children. The IRS has issued guidance on the tax treatment of health coverage for children under age 27 under the new health reform law. The new under age 27 rule, which went into effect March 30, 2010, applies broadly to employer-

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provided coverage or reimbursements, cafeteria plans, flexible spending arrangements ("FSAs"), health reimbursement arrangements ("HRAs"), voluntary employees' beneficiary associations ("VEBAs") and the above-the-line deductions for a self employed individual's medical care insurance costs.

State address estate planning uncertaintly. As of now, there is no estate or generation-skipping transfer ("GST") tax for individuals who die this year. There are issues as to how formula clauses in wills and trusts using estate or GST tax terms (e.g., "the applicable exclusion amount" or "the marital deduction") will be construed if the decedent dies in 2010. Several states have addressed this situation by enacting laws providing a special rule of construction under which formula clauses that refer to certain estate and GST tax terms generally will be constructed as referring to the Federal estate tax and GST tax laws which applied to estates of decedents who died in 2009. These statutes could impact the amount that will pass under one's will to a spouse and children.

* * *

If you would like to discuss these new tax law provisions and how they might affect you, please contact Ron Feuerstein at rfeuerstein@beankinney.com.

This newsletter was prepared by Bean, Kinney & Korman, P.C. as a service to clients and friends of the firm. The purpose of this newsletter is to provide a general review of current issues. It is not intended as a source of specific legal advice. © Bean, Kinney & Korman, P.C. 2010.

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