

# TRENDLINES

YEAR END 2011

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## RSSM

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## M&A TODAY

# IT COULD HAPPEN TO YOU

If your company is struggling with its profitability and battling to compete, the idea of expanding through a merger or acquisition may seem ridiculous. But that doesn't mean there isn't a larger business out there that may want to add your organization to its roster as part of a greater strategic plan.

Or maybe you've emerged as the leader of the pack in your market, and gobbling up a suitable company at an advantageous price could further cement your dominance. Whatever the case may be, it behooves every savvy business owner to stay up on the fundamentals of M&A — just in case it happens to you.

### Beyond retirement

Perhaps the first thing to cross any business owner's mind when the prospect of an M&A deal comes up is: Should I do this now? Whether you're a seller or a buyer, timing is everything.

So, as a seller, when is the right time? Well, retirement is the most obvious example. If you plan to, at least in part, live off the proceeds of the sale of your business after you retire, you'll need to start hunting for the right M&A deal well in advance of your bon voyage party.

Yet don't assume the perfect buyer will emerge right when you're ready to hang it up. You may find the ideal candidate a few years before your planned retirement date. In that case, you'll have to make the tough call as to whether to retire early or risk losing your suitor. On the bright side,

in many cases former owners can stay involved with the company as a consultant.

Of course, even when an owner hasn't been planning to sell the business anytime soon, an urgent need to sell can come up — especially these days. Shifting market conditions, obsolete product lines, outmoded technologies and lack of credit may be signals that it's time to move on.

Leadership conflicts can also be a glaring red flag. Do you spend more time fighting than working with your business partner? If so, a sale could be an extreme but necessary solution.

### Opportunity + capital

For buyers, timing is somewhat simpler. It's generally a matter of opportunity plus capital. That is, you encounter a suitable target to merge with or acquire and you have the finances to get the deal



done. But that doesn't mean it will always or even usually be an easy decision.

*If you spend more time fighting than working with your business partner, a sale could be an extreme but necessary solution.*

An M&A target must fit in with your strategic goals. You'll be spending a lot of time, money and resources on a deal. And, once it's completed, there will still be much work to do. (See "Don't forget about an integration plan" below.) So you've got to ensure that the business you're

buying will make you more competitive and profitable, not just briefly put your name in the news.

Due diligence is of paramount importance. That means not only fully grasping the target's finances and any legal issues involved, but also looking closely at the target's operations. Scrutinize its marketing and sales, production, and administration departments carefully. These functions can often hold deal-breaking pitfalls.

### **Taxes and sale structure**

As you might expect, Uncle Sam will want a piece of any M&A transaction. But not every business sale need be immediately taxable. Some arrangements may qualify for *tax-deferred* treatment. Examples include transactions in which the seller receives buyer stock or certain qualifying property in exchange for their stock or assets. Corporate or

## **Don't forget about an integration plan**

In any merger or acquisition, a large amount of work goes into establishing a sales price, doing the due diligence, making sure all the required legalities are in place and working out the terms for precisely how the money will change hands.

But let's say money matters are settled and a deal is in place. What then do buyers and sellers have to think about? In a word, integration. Whether one organization is consuming the other, or the two are merging together, how will they execute that union smoothly?

Granted, a seller could just wash his or her hands of the matter and let the buyer worry about it. But most departing business owners want to know that their employees will be in good hands and operations will move forward positively and productively.

To this end, an integration plan should be part and parcel of any M&A arrangement. And this plan needs to set the right tempo for the transition. Sometimes a buyer will finish the sale and immediately start shutting down divisions and laying off workers. As a result, remaining staff feel alienated and even angry, which hurts morale and productivity.

Then again, an integration that moves too slowly can leave workers confused and even frustrated. They might ask: "Where's the win-win we were promised? None of our problems are being solved!" The company may also start to bleed cash if the transition goes too slowly and redundancies get the better of the bottom line.

In M&A deals, timing is indeed everything. But so is tempo — the transition must move at the right pace. A carefully constructed integration plan can ensure this happens.

partnership/limited liability company (LLC) mergers may be eligible for tax deferrals as well.

Understandably enough, many parties to M&A deals favor the idea of a tax-deferred sale. But there are situations in which paying taxes upfront is the better way to go. For example, despite immediate taxability, cash-only sales are simpler and typically quicker to execute. Buyers typically favor a taxable sale to get a stepped-up basis in the assets, which can reduce future taxes.

If your company or one you're thinking about buying is structured as a corporation, you'll have to choose between a stock sale and an asset sale. Parties to an M&A deal often end up at odds here: Sellers look to stock sales to get favorable capital gains treatment. Meanwhile, buyers prefer asset sales to maximize future depreciation write-offs and to limit legal liability. (The buyer

assumes the known and unknown liabilities in a typical stock deal.)

Buyers also tend to frown on stock sales because they'll have to deal with the carryover basis in the assets, which may raise their future tax liability. Conversely, stock sales of C corporations appeal greatly to sellers because the departing owner(s) may avoid double taxation when they sell the assets and then distribute cash to shareholders.

### Deal ready

The uncertain economy has put a dent in the frequency of M&A deals. But plenty are still going down and much depends on the industry in question. Even if a business sale or purchase is the furthest thing from your mind at the moment, keeping your company in "deal ready" shape can strengthen your leverage should an intriguing opportunity arise. □

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# THE WHEN AND WHAT OF CHARITABLE DONATIONS

*W*ith one year ending and another beginning, gift giving may be on your mind. And that may mean not only giving to family and friends, but also donating to the qualified charities of your choice.

To help you get a better grasp on the tax ramifications of your prospective good deed, let's look at the "when" and "what" of charitable giving.

### Assessing your options

The first major factor to consider is *when* to give. If you donate to charity through your will or living trust, your estate typically can claim a charitable deduction. If you donate during your lifetime, the donation's value is no longer a part of your estate, so the gift yields the same estate tax benefit as a bequest. But in addition, gifts to qualified charities



## Stocking up

Then there's the "what" of charitable giving. Typically, it's best to give long-term appreciated securities (such as publicly traded stock, mutual fund shares and closely held stock held more than one year) because these donations may be more tax-efficient.

For example, if you sell stocks that have increased in value since you purchased them, you'll have to pay income tax on the capital gain — even if you then donate the proceeds to charity. But you can avoid the capital gains tax if you donate the shares themselves to charity. Plus, the charity generally won't incur any tax if it sells

the shares, though certain charities (such as private foundations) will be subject to a minimal tax.

You can deduct the shares' full fair market value on the day you make the transfer. (If you donate closely held stock, you may need to obtain a qualified business valuation.) Beware, however, that donations of appreciated assets are subject to tighter AGI limits than other types of donations.

made during your lifetime entitle you to a charitable deduction for income tax purposes.

Be aware that your income tax deduction may be limited, based on your adjusted gross income (AGI), the type of asset you donate and the nature of the organization receiving the gift, among other factors. Charitable gifts that exceed the AGI limits generally can be carried forward for up to five years.

If you're concerned about your future financial needs, it might not be wise to make large gifts during your lifetime. Making charitable gifts through your will or living trust allows you to retain access to the assets during your lifetime, and the estate tax charitable deduction generally is unlimited. But you'll forgo an income tax deduction.

Alternatively, consider giving during your lifetime using a charitable remainder trust (CRT). A CRT allows you to make a gift today and receive an income tax deduction determined by the expected amount that will go to the charity in the future (when the CRT terminates). You retain the right to a stream of payments from the trust, which may alleviate some financial concerns about making the gift.

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You may take advantage of this strategy even if you don't want to immediately dispose of your stock. How? Donate your appreciated stock to charity for the tax benefit and then buy back the same stock with other funds. When you later sell those shares, your tax basis will be higher than it

would have been, reducing your capital gains tax. Other types of gifts may include:

- ✓ Real estate,
- ✓ Life insurance,
- ✓ Retirement plan assets, and
- ✓ Personal property such as automobiles, artwork and antiques.

Be mindful that, if you're donating personal property, you can deduct only your cost basis and not the fair market value of the property unless the charity will use the property in connection with its stated mission.

### Working to anticipate

Making a sizable donation is a great way to end a year — or start a new one. Just be sure to work with your financial advisor to anticipate how Uncle Sam will treat your benevolent bequest. □

## MONEYLINES: NEWS BRIEFS FOR BUSINESSES

**Recent changes to ADA regulations heighten employers' risk.** Getting hit with a disability lawsuit could seriously harm any company's bottom line. And the legal definition of "disability" isn't what it used to be. Earlier this year, the Equal Employment Opportunity Commission amended its Americans with Disabilities Act (ADA) regulations to harmonize with the ADA Amendments Act of 2008. The new regs broaden the definition of "disability," which may lead courts to more readily find merit in ADA-related cases brought before them.

**IT staffers surely find CFOs' lack of faith disturbing.** Virtually no business can get very far these days without a strong grasp of technology. Unfortunately, many CFOs aren't all that confident in the work of the employees and others who provide IT support. Or so indicates a 2011 collaborative survey of 344 CFOs conducted by Financial Executives International and Gartner. It found that only 18% of responding CFOs believe their "IT service levels meet or exceed business expectations." If you feel likewise about your IT staff or provider, perhaps make alleviating this disconnect one of your 2012 objectives.

**How financially stressed are your workers?** Employees worried about money can be less productive on the job and more prone to taking sick days. The good news: In the first quarter of 2011, only 21% of workers surveyed by financial educators Financial Finesse reported having high or overwhelming financial stress. That's down from 32% in 2010. You might survey your employees to see whether they report similar results now at year end. For those who are stressed, no- or low-cost money management seminars and regular retirement account updates may help.



# SOON-TO-BE RETIREES PONDER DOWNSIZING THEIR HOME

Gail and Allen love their historic Victorian home. It was a “dream come true” purchase made, for better or worse, right before the real estate bubble burst. But with its multiple floors and steep staircases, the house may not suit them in retirement. Both have health concerns that could affect their future mobility, and the upkeep is considerable.

So they visited their financial advisor to discuss the notion of buying a smaller home soon after they retire in the near future. Their advisor began by noting that it was good Gail and Allen didn’t need to move right away, because the idea wasn’t necessarily a slam dunk.

## Now and later

First, they’d have to think through how a home purchase would affect them financially — both immediately and in the long term.

Would they have enough cash for a down payment? They’ve yet to pay off their mortgage, and the couple was unclear on just how much equity their Victorian had lost. Lenders are typically asking for 20% up front, which has some retirees dipping into their savings. This money may be better off staying in their retirement funds to continue growing tax-deferred (or, in the case of a Roth account, tax-free) or being set aside for medical costs.

Second, will Gail and Allen be able to afford home ownership during retirement when their income is lower? Even a smaller home will require mortgage payments, maintenance expenses and property taxes. They could look into a condo, but these often feature newer amenities, as well as association fees, that can make them unexpectedly expensive. The couple might find it more economical to rent.

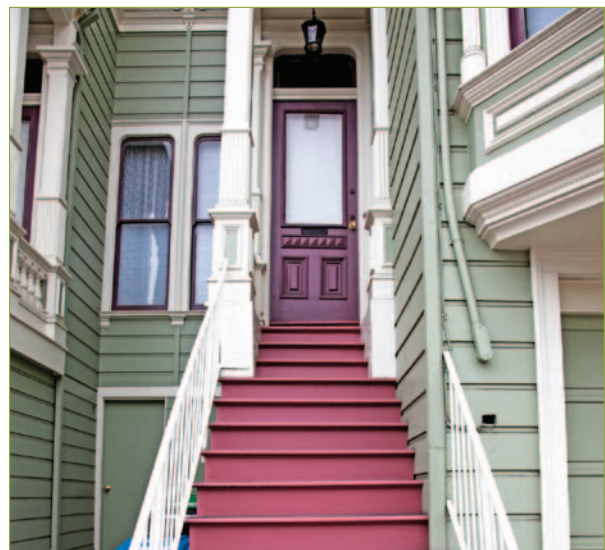
## Other matters

Another issue is the potential difficulty of getting a mortgage for the smaller home. Although lenders are forbidden from discriminating against borrowers on the basis of age, the couple will face very strict lending requirements. They should expect to have their cash flow, debt load and credit history scrutinized.

On a more positive note, as homeowners, the couple could continue to enjoy certain tax breaks. These include the property tax deduction and the mortgage interest deduction.

## A weighty subject

The tax benefits and other advantages of homeownership were enough to convince Gail and Allen to put their house up for sale and see what offers the market generated. But they valued their financial advisor’s cautionary advice and promised to check in with him regularly regarding the progress of the sale. □





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Our extensive and practical experience assists our clients to operate and expand successfully, while minimizing taxes and retaining more of their profits.

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