Brennan & Associates

5450 Germantown Avenue
Philadelphia, PA 19144
Tel: (215) 951-5585 Fax: (215) 844-4950

CLIENT'S tax & financial UPDATE

VOLUME **32** / NUMBER **4**

MARCH - APRIL 2010 ISSUE

A tax, business, and financial planning newsletter for our clients and friends

How To Sell Your Business

There are two equally important stages in the successful sale of a business. The first stage is preparing the business for sale and the second is finding a buyer and getting the best possible price.

Preparing your business for sale. This stage is critical and should begin well in advance of the time you actually put the business up for sale. During this period, your goal should be to establish a solid history of profitability since the first thing any buyer looks at will be profits. Although it's up to the buyer to judge potential profitability, it's your job to clearly demonstrate past and present profitability.

To establish an impressive track record, you may have to abandon some common business practices. For example, you may be able to improve your profit picture by putting less emphasis on tax savings strategies.

A business buyer will also look at key employees—those who are responsible for the success of your business. Make a strong effort to retain these employees, even if it means offering them extra incentives to stay with the business, at least up to the time it's sold.

Setting a price and finding a buyer. There are several factors that will determine what your business is really worth. One factor that's sometimes overlooked is whether a business outperforms others in the same industry.

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taxPOINTS

Education savings. Contributions to a state-sponsored "Section 529" college savings plan and/or to a Coverdell Education Savings Account can earn investment returns that are tax free when used to pay education costs. Also, up to $5,250 received from an employer's qualified education assistance plan can be taken tax free when used to pay for the employee's education.

Home sales. Up to $250,000 of gain can be taken tax free on the sale of a home when you've owned it and used it as a primary residence for two of the prior five years. The limit is $500,000 on a joint return.

Loophole: Donate appreciated long-term stock instead of cash to your favorite charities.

When you do this, you can deduct the full fair market value of the shares and owe no capital gains tax on the stock's buildup in value since you bought it.

Example: You own 100 shares of stock purchased 10 years ago for $20 per share. When you donate the shares, now worth $50 each, to charity, you deduct the full $5,000 fair market value – not your $2,000 cost. You also avoid paying capital gains tax on the $3,000 of appreciation in the shares.

Two Ways to Deduct Car Expenses

If you use your car for business purposes and your employer does not reimburse you, there are two ways you can deduct your car expenses. Use the method that's best for your individual situation.

The actual cost method. To use this method, you must keep detailed records of all business-related car expenses. These include gas, oil, maintenance, car washing, insurance, repairs, interest on your car loan, supplies, tires, automobile club dues, depreciation, and taxes.

The mileage method. To take deductions, you must keep a record of the number of business related miles you travel, your point of departure and your destination, and an explanation of the business purpose of your auto travel. You are allowed to deduct a specific amount per mile. You can also deduct miscellaneous expenses such as parking charges and tolls, but you must be able to substantiate them.

Reduce The Cost Of Unemployment Payroll Taxes

If an employee resigns, ask for a written letter of resignation that explains the reason why the employee is leaving the company. Reason: If the former employee files for unemployment compensation and you want to challenge the claim, the letter can support your challenge, which could help you lower the cost of unemployment payroll taxes.

Hidden Danger In Your Accounts Payable System

An unscrupulous supplier might bill you at a price which is higher than the price on your purchase order in the hope that the over-billing won't be noticed because you have a poor accounts payable system. To protect yourself against this possibility, make sure that your accounts payable employees check every incoming invoice against the original purchase order and initial the invoice to show that it has been approved for payment.

If an invoice price is higher than the purchase order price, it's perfectly legal to pay the lower purchase order price. Under the Uniform Commercial Code (UCC), a vendor must abide by the terms of a purchase order if the vendor delivers any portion of the merchandise without objecting to the purchase order terms.

What to Do If You Can't File on Time

You can get an automatic extension until October 15, 2010 to file your tax return. All that's necessary is that you notify the IRS by filing Form 4868 no later than April 15, 2010.

Important: An extension of your filing date is *not* an extension of the time when you must pay your taxes. You must estimate the amount of tax you owe and attach a check for that amount to Form 4868 and mail it by April 15. If you don't pay your tax until the extended due date, you'll be charged interest and penalties for the late payment.

Try to estimate you tax as accurately as you can. If you underestimate your tax bill, you'll be charged interest on the underestimated amount, and if you underestimate by more than 10%, you'll be charged a penalty as well as interest.

You generally cannot get a filing extension beyond six months, but there may be an exception if you are living out of the country.

How to Borrow Interest-Free from Your IRA

The rules for taking money from an IRA are quite clear. Any amount you withdraw is subject to income tax in the year in which the money is distributed to you. If you receive distributions before you reach the age of 59-1/2 (except for death or disability), those distributions are subject to a 10% penalty.

However, there is a little-known exception to these rules that lets you withdraw any amount you wish from your IRA tax-free and penalty-free. In effect, you can use your IRA as your own private loan company and borrow from it without paying interest.

Be very careful, however, because you must return the funds to the IRA from which you withdrew them or you must rollover the withdrawn funds into another IRA within 60 days of the date you withdrew the money. Furthermore, you can only "borrow" from your IRA once a year using this technique.

Get All Your Deductions For Job Search Expenses

You can deduct the costs of looking for a new job as deductible miscellaneous expenses subject to the 2% of the Adjusted Gross Income limit. Even if you do not wind up with a new job, you can still deduct these expenses:

- Newspapers and business publications that you buy for their employment ads.
- Fees you pay to career consultants, recruiters, employment agencies, and resume writers.
- Resume preparation costs such as typing, printing, envelopes and postage.
- Miscellaneous transportation costs such as taxi fares or parking costs for job interviews.
- Telephone calls made in connection with your job search.
- Out-of –town travel expenses including transportation, hotels, and 50% of the cost of all meals.
- Legal and accounting fees for tax advice about employment contracts.

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How To Sell Your Business

You can get information about typical industry performance from trade associations and business publications. If your business outperforms others, it's worth more.

A complete, well-prepared financial statement will speak for itself, but the intangible assets of your business are also worth money and you should discuss them and explain their value to a potential buyer. Goodwill is responsible for your company's financial stability and growth potential. Proven marketing ability, a solid customer base, and good management practices also add to the value of your business. These intangibles can have a very positive influence on a prospective buyer.

And don't overlook hidden strengths of the business. For example, be sure to point out any tangible assets that are carried on your books at less than market value.

The key to finding a buyer is networking. Get the word out that your business is for sale through your accountant, your lawyer, your banker, and your business associates. Approach potential buyers within your industry either directly or through third party "finders". Often, the best prospective buyers are companies who sell through similar distribution channels or whose product lines or production capabilities can be improved by an acquisition. And the possibility of an increased market share may turn a competitor into a buyer.

Be sure to work closely with your accountant before you structure a sale. The tax ramifications of a business sale are often as important to the buyer as they are to a seller.

How to Head Off a Financial Crisis

Many financial crises can be avoided if businesses pay attention to certain warning signals. Here are the most common signs that a financial crisis is approaching:

- Sales and profits consistently fall short of projections over a period of time.
- Inventories show a steady growth pattern.
- Indebtedness climbs.
- Available capital declines as cash flow problems mount.

Each of these problems indicates that a company is heading for real trouble and that prompt and decisive action must be taken.

Institute cash flow controls. Isolate the areas of the business which are draining cash from the company. Don't get bogged down on small items that prevent you from seeing the big picture. It's not uncommon for a company to encounter cash flow problems because a major segment of the business simply isn't profitable. If you discover that situation in your business, don't hesitate to scale down or even eliminate the unprofitable segment.

Slim down fat inventories. High inventory levels mean that sales are off or the purchasing is mismanaged. Cure this situation by selling excess inventory and installing controls to make sure that purchasing levels are based on current sales, not projected sales.

Speed up collections. Improved billing procedures mean faster invoicing and earlier collections, so if your company can ship most of its orders promptly, prepare invoices before the goods are shipped. Invoice more frequently. Finally, negotiate extended terms of payment with major vendors.

Review all product lines. Consider discontinuing any products that are not profitable. Many businesses fail to realize that a deliberate reduction in sales can mean a return to profitability.

Reduce overhead immediately. Cut the workforce to the lowest level possible. Make sure that the employees who remain can make a direct contribution to solving the company's problems.