

## ***Business Start-Up***

### **How To Begin: Checklist for Forming an Ohio Corporation**

1) Call the secretary of state at (614)466-3910 or toll free at (877)767-3453 to determine if the proposed corporate name is acceptable. It is possible to e-mail the Business Services Division from the Ohio Secretary of State's Web site at [www.sos.state.oh.us/sos](http://www.sos.state.oh.us/sos) ; click "business filings," and you can conduct your own search on the secretary of state's Web site. The proposed name must be "distinguishable upon the records" of the secretary of state. A name is not considered to be distinguishable from another name if the only difference is:

- a) Reversing of words (*e.g.*, Fast Copy, Copy Fast);
- b) Use of Arabic numbers or Roman numerals (*e.g.*, Jim's Sales I, Jim's Sales II);
- c) Use of possessives (*e.g.*, Thompson Auto Body, Thompson's Auto Body);
- d) Phonetic spelling (*e.g.*, Quick, Kwik);

2) Determine availability of the proposed corporate name in any other states in which the business will operate.

3) File the articles of incorporation with the Ohio Secretary of State, Business Services Division, P.O. Box 670 Columbus, Ohio 43216. Expedited filing is permitted by paying an additional \$100 fee and sending the articles and the fees to: Secretary of State, P.O. Box 1390, Columbus, Ohio 43216.

a) You must use Secretary of State Form 532.

1) The name of the corporation must end with "Company," "Co.," "Corporation," "Corp.," "Incorporated," or "Inc."

2) The articles must indicate the corporation's principal office—city, village or township and county.

- 3) The articles must state the number of authorized shares that can be issued and their express terms. NOTE: The number of shares authorized determines the filing fee.
- 4) If the corporation plans to have an initial stated capital, it must be included.
- 5) You may appoint the initial board of directors in the articles.
- 6) The articles must be signed by all incorporators.
- b) The Original Appointment of Agent is included in the Secretary of State Form 532.
  - 1) The statutory agent must acknowledge and accept the appointment.
  - 2) The statutory agent's address must contain a street address and zip code. Post office boxes are not acceptable.
  - c) The filing fee must be in the form of a check made payable to the secretary of state. The minimum fee for filing the articles is \$125. This minimum fee permits the issuance of 1,500 shares. See *Ohio Revised Code* Section 111.16(A)(2) for the appropriate filing fee if more than 1,500 shares are to be issued.
  - d) The secretary of state's office will not return the articles after filing. Send a photocopy of the articles and retain the original articles.
- 4) Incorporators, or the directors if named in the articles, should start a minute book by acknowledging the filing of the articles and including the original of the filed articles.
  - a) Incorporators, or the directors if named in the articles, should authorize the issuance of shares.
  - b) The investors should sign a *subscription agreement*, the agreement in which the investor agrees to buy the shares for a given price.
  - c) The incorporators, or the directors if named in the articles, may set the value of noncash assets in payment of the subscriptions.
  - d) The incorporators, or the directors if named in the articles, accept the subscriptions.
  - e) The incorporators must give notice of the first shareholders' meeting.
- 5) Consider becoming a "Subchapter S" corporation for federal and state tax purposes. See Sections 1362 et seq. of the *Internal Revenue Code*.
  - a) Use IRS Form 2553. File with the Internal Revenue Service Center, Cincinnati, Ohio 45999 within the 16th day of the third month of the beginning of the tax year.
  - b) Shareholders and the corporation must file a notice of the subchapter selection with the Ohio Department of Taxation.
- 6) If the business will operate under a name other than its corporate name, a Report of Use of a fictitious name must be filed on Form 534 with the Ohio Secretary of State, P.O. Box 670, Columbus, Ohio 43216. There is a \$50 fee to file this form.

- 7) A trade name may be registered with the secretary of state by completing Form 534, and sending it, along with a \$50 filing fee, to the address provided above in item 6.
- 8) Make sure your business complies with the Ohio securities laws. The most common exemption from the Ohio registration requirements for small businesses is a small business equity investment to ten or fewer investors (*Ohio Revised Code* Section 1707.03[O]). To comply with this exemption, the subscription agreement must include statements that: 1) the purchaser is aware that no market may exist for resale of the securities; 2) the purchaser is aware of any restrictions on transfer of the securities; and 3) the purchaser declares that the purchase of equity is for investment purposes and not for redistribution. If there are non-Ohio investors, check with their resident state security regulator.
- 9) Make sure your business complies with federal securities laws. Registration is required unless an exemption is available. Following are the two most common exemptions for small businesses:
- a) Intrastate exemption (see Securities and Exchange Commission Rule 147);
  - b) Private placement exemption (see Regulation D of the Securities and Exchange Commission).
- 10) Obtain the taxpayer identification number from the Internal Revenue Service. Submit Form SS-4. See the procedure set forth on the IRS Web site: [www.irs.ustreas.gov](http://www.irs.ustreas.gov). Note that any person filing a Form SS-4 other than a corporate officer must file an IRS Form 2848 with the Form SS-4.
- a) By filing the Form SS-4, the corporation is automatically pre-enrolled in the Electronic Tax Payment System.
  - b) By filing the form SS-4, the corporation will receive the IRS Circular E Employee's Tax Guide – Forms for Payroll.
- 11) Take the following action at the first shareholders' meeting or by written consent of all shareholders.
- a) Elect directors.
  - b) If the directors named in the articles have not done so, the shareholders should adopt the regulations for the internal government of the corporation.
  - c) Consider adopting a close corporation agreement (see *Ohio Revised Code* Section 1701.591).
  - d) Set value for any non-cash payments by investors to the corporation.

- e) Consider adopting a shareholder's buy and sell agreement.
- f) Set the fiscal year for the corporation.

12) Take the following action at the first meeting of the board of directors or by written consent by all directors.

- a) Elect officers.
- b) Set compensation of key employees.
- c) Consider adopting benefit plans.
- d) Consider adopting group term life insurance plan (see *Internal Revenue Code* Section 79).
- e) Consider adopting accident and health insurance plan (see *Internal Revenue Code* Section 105[b]).
- f) Consider adopting medical reimbursement plan (see *Internal Revenue Code* Section 105[b]).
- g) Consider adopting a death benefit plan (see *Internal Revenue Code* Section 101[b]).
- h) Consider adopting a Section 1244 plan. This allows the stockholders to take an ordinary tax loss rather than a capital loss if the business fails and the stockholders lose their investment (see *Internal Revenue Code* Section 1244).
- i) Adopt a resolution for leasing business space.
- j) Adopt a resolution for the purchase of any real estate.
- k) Set up a bank account by adopting a bank-provided resolution.

13) Consider requiring key employees to execute employment agreements with covenants not to compete.

14) Issue stock certificates or transaction statements for paid shares.

15) Consider adopting policies about the following issues to protect the company, the directors and the executives:

- a) Sexual harassment;
- b) Non-discrimination;
- c) Trade secret protection;
- d) Company ethics (e.g., corporate gifts, anti-kickbacks);
- e) E-mail, computer and Internet use;
- f) Compliance with environmental laws;
- g) Compliance with the anti-trust laws;
- h) Compliance with the worker safety rules;

- i) Development of procedures to prevent hiring of illegal aliens; and
- j) Political contributions.

16) Obtain the following posters to be placed conspicuously in the workplace:

- a) Ohio Civil Rights (contact the Ohio Civil Rights Commission, Education and Community Relations, 111 East Broad Street, 3rd Floor, Columbus, Ohio 43205-1371);
- b) Fair Labor Standards Act – Minimum Wage poster;
- c) Employee Polygraph Protection Act – poster advising employees of federal rights when confronted by a request from an employer to undergo a lie detector test;
- d) Rights of employees under the Family and Medical Leave Act poster;
- e) Posted notice of company's anti-discrimination policy and anti-harassment policy (sex, race, national origin, etc.);
- f) Federal Occupational Safety and Health Act (OSHA) poster (states the rights of employees under OSHA);
- g) Federal Equal Employment Opportunity Commission poster;
- h) Ohio Wage and Hour requirements poster (See Web site: [www.com.ohio.gov/laws/docs/laws\\_minimumwageposter2009.pdf](http://www.com.ohio.gov/laws/docs/laws_minimumwageposter2009.pdf) ).

17) Become an Ohio income tax withholding agent. File Form IT-1, Application for Registration as an Ohio Withholding Agent, with the Ohio Department of Taxation. See the Ohio Business Gateway for Electronic Filing ( <http://business.ohio.gov/efiling> ) or the Ohio Department of Taxation ( [www.tax.ohio.gov](http://www.tax.ohio.gov) ).

18) File Form JFS 66300, Report to Determine Liability (Unemployment Compensation), with the Ohio Department of Job and Family Services, Contributions Section, P.O. Box 182404, Columbus, Ohio 43218-2404 or go to Ohio Business Gateway ( <http://business.ohio.gov> ) or the Ohio Office of Unemployment Compensation ( [www.jfs.ohio.gov/ouc](http://www.jfs.ohio.gov/ouc) ).

19) File Form U-3 Application Coverage with the Ohio Bureau of Workers' Compensation. It is possible to apply online. See [www.ohiobwc.com](http://www.ohiobwc.com) .

20) File the commercial activity tax registration Form CAT-1 with the Ohio Department of Taxation ( [www.tax.ohio.gov](http://www.tax.ohio.gov) ).

- 21) Obtain a vendor's license from the county auditor. This is needed for compliance with Ohio sales tax on goods. Use Form ST-1. The filing fee is \$25. (Go to [www.tax.ohio.gov](http://www.tax.ohio.gov).)
- 22) If selling services, your corporation must register as a service vendor for the sales tax on services. Use Form ST-1S and file with the Ohio Department of Taxation, Registration Unit, P.O. Box 182215, Columbus, Ohio 43218-2215. There is a \$25 filing fee.
- 23) Form JFS 07048 must be filed with the Ohio New Hire Reporting Program by mail at P.O. Box 15309, Columbus, Ohio, 43215-0309, by FAX at (888)872-1611 or online at [www.oh-newhire.com](http://www.oh-newhire.com).
- 24) Obtain from local authorities the information and forms for local income tax compliance.
- 25) Information can be obtained from the following state agencies:
- a) 1st Stop Business Connection: (800)248-4040 or (614)466-4232 or [www.development.ohio.gov/edd/1ststop](http://www.development.ohio.gov/edd/1ststop));
  - b) Ohio Secretary of State (614)466-3910;
  - c) Ohio Department of Taxation: (888)405-4089;
  - d) Ohio Department of Securities: (614)644-7381, or (877)767-3453.
- by Jason C. Blackford, an attorney with the Cleveland firm, Weston Hurd LLP.

### Buyer Beware: The Steps to Purchasing a Business

If you are looking to buy or acquire a business, you will need patience, honed detective skills, legal and accounting advisors, and attention to every detail. The process of buying a business is a negotiation between the seller and the buyer, with both looking out for their own interests, as well as the future of the business—but for different reasons.

As the potential buyer, it's important to consider the seller's motivation to sell: Is it retirement? Or does seller foresee changes in the market place and have an aversion to putting more capital at risk? Knowing the reasons for the sale will help a buyer prepare an offer, including whether to purchase the assets of the business or the stock. As the buyer and seller negotiate through the sale, there are key documents to consider prior to the definitive agreement, including:

**Confidentiality agreement:** In order to receive basic information about seller, the buyer signs a document agreeing to use the information revealed only for the purpose of considering buying the business. Particularly, if the potential buyer is a competitor of the seller, the agreement may also preclude buyer from hiring seller's employees for a period of time, if the sale does not occur.

**Letter of intent (LOI):** This is generally a non-binding offer for the business. Buyers prefer a short LOI, seeking to delay negotiations of difficult issues such as risk allocation and seller's indemnification obligations, until the definitive agreement. Sellers prefer a more detailed LOI, as their greatest leverage is before its execution. Many times, sellers can be talking to multiple potential buyers prior to execution of a letter of intent. The signed LOI generally contains a provision giving the potential buyer exclusivity on negotiations for a 60- to 90-day period. Since disclosure of a potential sale, followed by no sale can cause morale problems for seller's employees and leave the seller with a reputation as damaged goods, the seller wants as many details resolved in the letter of intent as possible. Additionally, if there are roadblocks to the sale, the seller will want to know them as soon as possible to reduce legal fees and time commitment to the failed transaction.

### **Due diligence:**

Following execution of the confidentiality agreement, buyer conducts preliminary due diligence—an analysis of seller's business and financial results. The analysis at this stage determines whether buyer remains interested and establishes the potential price. Following execution of letter of intent, the buyer completes due diligence, which may include talking to key customers, suppliers and personnel. Due diligence is designed to provide the buyer a full understanding of the risks and liabilities of the business. Many times, buyer revises its bid

based

on information generated during due diligence.

As a buyer, you need to ask yourself what key assets you want to acquire in the purchase of the

business: a patent or important license, the seller's employees, key customer contracts or supply

agreements, or equipment. If the documents are drafted to accomplish the purchase of the key elements of the business and to allocate the risks for past and future events in a manner you,

as

the buyer, understand and accept, the purchase is being done correctly. Finalize the deal.

*—by Michael A. Ellis, an attorney with the Cleveland office of Porter Wright Morris & Arthur LLP.*

### The Business Acquisition Checklist

One important way a small business can grow is by merging with or acquiring another company.

An owner considering a merger or acquisition should take as many of the following steps as possible to evaluate the target company before deciding whether or not to proceed.

### Financing Your Business

Maybe you have been able to finance the start-up and early growth of your business through the

use of your own capital. But now, in order to sustain or grow your business, you need additional

financing. What financing vehicles are out there for the average “lifestyle” business that does not

expect to be the next Google?

The most commonly used financing options available to your business can be grouped into six categories:

1) credit cards;

2) angel investors;

3) venture or private equity financing;



- 4) factoring;
- 5) asset-backed lending; and
- 6) working capital lines of credit.

Many entrepreneurs finance initial business growth through the use of personal, uncollateralized credit cards. While images of plunging personal credit ratings, high interest rates and unmanageable debt may make credit card financing unattractive, it should not be ruled out. A number of national organizations offer small business owners credit cards with low, fixed interest rates and attractive payment terms.

Angel investors are high net worth individuals seeking better returns than offered through more conventional investment vehicles. They enjoy investing money, and sometimes time, in attractive businesses. There are many angel investors throughout Ohio and the Midwest. Moreover, individuals in group angel funds sometimes invest their own money through *sidecar* investments.

Business should be aware, however, that strings may be attached to angel funds. Venture and private equity funds abound, but the trick is to find one that would be attracted to your type of business. Think carefully about who to approach and what type of debt and/or equity arrangement each might seek. Some funds require you to relinquish ownership control. Most want some vote in all important business decisions and all want to thoroughly understand your *exit strategy*. Moreover, most venture and private equity funds must exit your business within a short time period and return their capital to their respective investors. There are three exit options:

1) sell the company; 2) have a public offering; or 3) undertake a recapitalization. Without an exit strategy, you may have trouble attracting fund investors.

Factoring is a viable option for some, particularly those businesses with account receivables that are slow to be paid and, therefore, hurt cash flow. A factoring company buys your receivables at a particular percentage of their stated value (say 80 percent). Some factoring arrangements allow the factoring company to “put” the receivables back to you should they fail to collect. While the cost is certainly higher than traditional bank financing, it is often a good short-term arrangement

for the business experiencing less than stellar credit, poor cash flow or rapid growth. Bank financing, be it asset-based or working capital, is the most traditional financing vehicle and the most difficult to attract. Asset-backed financing may be available to the business owner who might not be able to attract a cash flow lender, but who has sufficient hard assets to cover the bank's credit exposure. Cash-flow lending requires a lender to study the company's financials and determine whether the business will remain cash-flow positive so it can repay the bank. As added security, lenders traditionally will secure all the business assets and may seek to secure personal assets.

An experienced advisor can assist you in negotiating the maize of financing options and help prepare and review the necessary documentation any financing entity will require from you before investing in your company.

*—by Thomas C. Washbush, an attorney with the Columbus firm of Benesch Friedlander Coplan & Aronoff.*

### **Preparation Can Improve Bank Loan Experience for Business Borrowers**

Whether you are starting or expanding your business, chances are you will need to ask a bank for financing. You may assume a bank will evaluate your business based on dollars and cents, but do you really know how bank lending officers evaluate loan applications? Are you aware of the importance of intangibles such as community standing, reputation, community benefit and your business's likelihood of repaying the loan?

You can assume that the lending officer and the bank want your business to succeed so you can repay the loan, but you should know that the bank (especially if it is community-based) also has an interest in your business's success because of its positive impact on the community. Before making an appointment with a loan officer, you should know what the bank is looking for

and be prepared to provide the necessary information.

### Information

You will need to provide the bank with the following:

- two to three years of business tax returns;
- two to three years of personal tax returns;
- a current financial statement;
- a year-to-date income statement and balance sheet on your business entity;
- a history of your business and/or a business plan. If the business is a start-up, then you will need to provide projections for the next three to five years and the basis for those projections.

### Collateral

Banks must make sure businesses have enough collateral to secure loan requests. To determine

whether your business has the necessary collateral, the bank will use the following criteria:

- If you are using commercial real estate for collateral, the bank will want to know that, based on the property's appraised value minus any current mortgages, your business owns at least 20 percent of the interest in the property.
- If you are using accounts receivable as collateral, then typically the bank will use the following formula: 100 percent of the receivable accounts, multiplied by the receivable collection rate, multiplied by 70 percent, minus any current liens against accounts receivable assets.
- If you are using equipment and furniture as collateral, the bank will credit between 80 and 100 percent of a new purchase or 70 percent of the asset value after depreciation is figured and minus any current liens against the equipment or furniture.
- If you are using cash assets, then typically the bank will consider 100 percent of the assets minus any cash asset liens.
- If you are using marketable securities (such as stocks or bonds) as collateral, then the bank typically will consider 70 to 75 percent of the portfolio's value and 65 to 70 percent of the mutual fund value, minus any current liens against your marketable securities.

### Analysis

The bank will consider the following questions when deciding whether to grant your business a loan:

- Is there sufficient collateral?
- What is the personal credit history, the *debt-to-income* ratio and the liquidity of the

business owners (*guarantors* of the loan)? (Typically, banks look for a business to have no more than a 40 percent debt-to-income ratio.)

- Does the business have sufficient cash flow to service the debt? To find out if your business has sufficient cash flow to cover a loan, you may wish to contact a lender, an accountant, or an attorney.

*—by Paul E. Peltier, an attorney and director of wealth management for Champaign Bank based in Dublin, and Timothy M. Oyster, a business banking officer for Champaign Bank. Updated by Jeffrey S. Rosenstiel, a partner with the law firm Frost Brown Todd LLC.*

### Should You Buy or Lease Your Business Assets?

Business owners often struggle with the issue of whether it is better to buy or to lease business assets such as vehicles, equipment, space, etc. Unfortunately, there is no one right answer. Rather, a business owner must look at a number of factors.

In many instances, an outright purchase of an asset makes more economic sense than a lease. A *lessor* who leases an asset to a business takes a risk, but also wants to make a profit, so risk and profit considerations are built into the lease price and paid by the *lessee* (the business). Obviously, a business owner can eliminate the lessor's profit by purchasing the asset directly.

#### When leasing makes sense

There are many situations in which the business owner is better off to lease an asset. Cash flow concerns may make leasing attractive. A lease generally requires less up-front cash and lower monthly payments, which can free up cash flow for other business needs.

Leasing also makes sense when an asset is only needed for a short period of time. Short-term leases work well for short-term asset needs and may be a smart decision when it is not known how long the business will need the asset. Another reason to lease is to avoid the risk associated with owning an asset.

Many business assets, especially high-tech equipment, are likely to decrease in value quickly. Many business owners are unwilling to assume this risk. A lease allows the business to pass this

risk on to the lessor.

### **When buying makes sense**

In general, it is more advantageous to purchase rather than to lease business assets.

Purchasing

assets will eliminate the lessor's profit, resulting in a lower overall cost for the business. Also, the

law requires fewer disclosures for leases than for purchase loans, and lease agreements may be

more complicated than purchase agreements or may contain undesirable limitations. Certain purchased assets (such as buildings) may provide equity for the business, and, over the long run,

purchased assets should allow the business to retain more profits.

### **Weigh tax considerations**

When determining whether it makes more sense to buy or to lease, a business must consider the

tax ramifications. This is especially true if the business is looking at purchasing a luxury automobile that is subject to special depreciation and lease expense limits. Congress passed tax

provisions a few years ago that limit the amount of depreciation that can be taken on many vehicles.

Similarly, there are some *income inclusions* that apply to more expensive vehicle leases. The amount reduces the lease expense deduction. Generally, the income inclusion rules are not as bad

as the depreciation limitations. In other words, leasing can have a tax advantage over purchasing a luxury vehicle.

—by *Bruce D. Bernard, Esq.*, tax strategist with *Bernard Law, LLC* in Worthington.

## **Retirement Plan Option for Small Employers May Make 401(k) Plan Affordable**

### **Q: What, exactly, is a 401(k) plan?**

**A:** A 401(k) plan is a type of profit-sharing plan under which employees can elect to defer a portion of their compensation. The employer may, but is under no obligation to,

match all or a portion of the employees' deferrals.

**Q: My employees would like my company to consider offering a 401(k) plan, but my business**

**is small. Is such a plan affordable for small business owners?**

**A:** Due to low employee contributions and relatively high administrative costs, 401(k) plans were not typically the most advantageous retirement plan option for many small business owners. However, plans can provide a significant design option that can benefit business owners at a relatively low employee cost. Although 401(k) plans previously allowed employees to defer a portion of their compensation to the plan, the owner's contribution was limited by the level of employee deferrals. Under Section 401(k)(12) of the *Internal Revenue Code*, the complex and costly nondiscrimination rules have been simplified by optional *safe harbor* rules.

Specifically, a business owner can defer \$16,500 in 2009 to a plan on his or her own behalf regardless of the level of participation by other employees, provided the employer makes a contribution on behalf of each eligible employee to the 401(k) plan equal to three percent of that employee's compensation. Alternatively, the employer can contribute a safe harbor basic matching contribution equal to 100 percent of the first three percent of compensation deferred by employees and 50 percent of the next two percent of compensation deferred (e.g., if the employee defers five percent of compensation, the matching contribution will be four percent of compensation). An *enhanced match* of a 100 percent match on deferrals up to four percent of compensation may also be substituted for the basic matching contribution. Stated another way, for a three or four percent employee cost, the business owner can obtain a significant contribution with administrative costs which should be significantly reduced from those with traditional 401(k) plans.

Further, an employee aged 50 or older can defer additional *catch-up* contributions into the 401(k) plan up to \$5,500 in 2009. The catch-up contribution is in addition to the normal \$16,500 limit. Thus, the maximum elective deferral for an employee aged 50 or older is \$22,000 (i.e., \$16,500 + \$5,500) for 2009. The dollars limits for both the elective deferral and the catch-up contributions will be adjusted for cost of living in future years.

**Q: What, exactly, are the benefits to a small business owner?**

**A:** The following example illustrates the significant benefits available to the small business owner. Assume the following: annual revenues are \$400,000, staff compensation is \$108,000, and owner compensation \$170,000.

EXAMPLE:

- 1) The owner has \$170,000 compensation.
- 2)  $\$170,000 \times 3 \text{ percent (safe harbor contribution)} = \$5,100$ .
- 3) The owner can defer \$15,500 (\$20,500 if aged 50 or older) to the plan because the safe harbor three percent contribution is satisfied.
- 4) Total for owner:  $\$5,100 + \$15,500 = \$20,600$  (or \$25,600 if age 50).
- 5) The employer cost for non-highly-compensated employees is three percent of compensation or \$3,240, *i.e.*,  $\$108,000 \times \text{three percent} = \$3,240$ .

Under a safe harbor 401(k) plan, the benefit to the business owner is as follows: for a staff cost of three percent or \$3,240, the business owner can receive a total retirement plan contribution of \$20,600 (\$25,600 if age 50) from a total contribution pool of \$23,840 or 86.4 percent (\$28,840 or 88.7 percent if owner is age 50 or older) of all monies put into the retirement plan by the business and the owner.

Additionally, employees have been provided with the opportunity to save for their own retirement through the 401(k) plan.

Due to the safe harbor rules for 401(k) plans, the administrative burdens for such plans have been reduced. With the availability of significant contributions to the business owner which, in practice, may not have been previously available, small business owners should consider changing both traditional profit-sharing plans and/or costly cross-tested plans into safe harbor 401(k) plans.

*—by Richard A. Naegele and William P. Prescott, attorneys in the Avon firm of Wickens, Herzer, Panza, Cook & Batista.*

### Key Considerations When Adding Private Equity to Your Portfolio

A private equity investment is an investment in a privately held company either made directly or,

more typically, through private investment funds. The investment fund professionals actively guide the companies the fund acquires to optimize their value.

Private equity seeks to earn a higher return than publicly-traded stock to compensate for the lack

of a public market to which the investment can be sold. Here are some things to consider when

adding private equity to your portfolio:

- 1) **Diversification.** Avoid “one-shot” deals where all can be lost.
- 2) **Quality sponsors.** It all gets down to an investment in people. Be proud of the character, integrity and judgment of the people in whom you are investing.

3) **Quality co-investors.** Similarly, ask yourself if you are proud to be among the investment group. Can you speak to the character, integrity, judgment *and investment acumen* of your co-investors?

4) **Simple, understandable products or services.** Do you understand what you are investing in? Compare an electric toothbrush with disposable brushes to a free space, optical transceiver (whatever that is). If you do not understand it, you probably should not invest in it.

5) **Use of proceeds.** Understand how your money will be spent. For pure research and development? To test a product? To commercialize a proven product? To enrich the promoter?

6) **Projected return.** As Yogi Berra said, "If you don't know where you're going, you'll probably end up there." You should know the projected return and the risks assumed in trying to achieve it. Higher risk investments should yield higher returns—annualized Internal Rate of Return of 15-30 percent. If less is projected, you should probably not bother. If more is projected, you should probably run for cover.

7) **Legal rights.** Before committing to invest, understand your rights (and obligations) as a minority shareholder or limited partner with respect to, among other things,

- management fees and carried interests;
- dilution;
- distributions;
- capital calls;
- transfers of interests;
- tag-along/drag-along rights;
- registration rights.

—by Joe Juster, chair of the General Corporate Group at the Cleveland office of Calfee.

## Bill Collection: How To Get the Money You're Owed

***Q: I own a small business and my accounts receivable increase every month. I have sent my***

***customers statements and many sternly worded letters to little effect. What can I do?***

**A:** You can begin collection proceedings against your customers by first getting a judgment in court, and then *executing* on that judgment by garnishing bank accounts or wages, filing liens against their homes, or ordering certain assets to be seized.

***Q: If I have decided I have no choice but to sue my customers, what should I do next?***

**A:** It may be easier to retain an attorney to file these lawsuits, but if you have only a few customers to sue and the amount you are owed is small enough, you might be able to file a lawsuit yourself in small claims court.



***Q: If I sue my customers and receive judgments against them, they will be forced to pay me, won't they?***

**A:** Many people do not realize that a judgment is only an official acknowledgment that money is owed to you and not a directive for money to transfer hands. It is your job to try to collect that money. The easiest way to do this is to garnish the debtor's bank accounts or wages. To garnish someone's wages, you must file paperwork asking the court to seize the money from the judgment debtor's bank account or wages. The debtor, in turn, will have a chance to be heard by the court before any garnishment is granted.

***Q: How does the wage garnishment work?***

**A:** A person's wages can be garnished only up to 25 percent per pay. If, however, the person is paying other court-ordered deductions such as child support, the amount that can be garnished will be reduced. Garnishments are continuous orders, meaning that once you file the paperwork, employers must withhold funds from an employee's paycheck until your judgment is satisfied. Unfortunately, if another creditor is already garnishing the debtor's wages, you may have to wait as long as six months until the other garnishment is complete.

***Q: What other property can be garnished?***

**A:** In addition to wage garnishment, a debtor's real and personal property is also subject to collection, including interests in residential property, motor vehicles, and household items. However, recent changes to Ohio's exemption laws have increased protection for debtors. Specifically, the new law significantly increased the dollar amount of already existing exemptions for certain categories of property that an Ohio debtor may hold exempt from execution and garnishment. For example, the new law exempts from collection a debtor's interest in one motor vehicle in the amount of \$3,225. Previously, the exemption was \$1,000.

***Q: Are there any other options for collections?***

**A:** Yes. For instance, you may take your judgment and file it as a lien against a person's house and foreclose upon it. Also, you may ask the court to seize tangible items (e.g., jewelry, computers, equipment) and sell them at auction, then give you the proceeds. These are fairly complex procedures which are difficult to do without a lawyer's advice.

*—by Christopher Ernst and Nellie So, attorneys with Bricker & Eckler LLP. Mr. Ernst is in the Cleveland office and Ms. So is in the Columbus office.*

### A State Tax Time Bomb

You just finished reading a memo from your company's treasurer advising you that a southern state had billed the company for six figures worth of back taxes, interest and penalties dating back to 1989. To make matters worse, he told you that the company had also received questionnaires from two more state revenue departments indicating that they thought your company may be "doing business" in their states.

How can we owe money to these states? We don't have offices or employees in those states. Did not one of our advisors tell us that we were engaged in interstate commerce and, therefore, not subject to such taxes?

The situation becomes more complex over the next few weeks as the company receives questionnaires from several more states. Another state has sent you a bill, which is larger than the first. How far back can they go and how do they know about us?

Unfortunately, many small companies are beginning to experience events similar to what has just been described. What formerly was a non-issue for small- and medium-sized businesses has become an expensive and frightening nightmare. What is going on and why does it seem to be getting worse?

As in every other area of life, state and local governments require money to operate. In order to effectively increase revenues, governments must either increase tax rates or do a better job of collecting taxes that it believes are owed. Accordingly, over the last few years, two trends have occurred with regard to business taxes. State and local governments have pressed for court interpretations that would allow them to tax companies doing business in interstate commerce.

At the same time, those governments are devoting more resources toward collecting their taxes. Courts appear to be moving in the direction of allowing states to tax companies based upon "economic presence" in the state even when the company in question has no physical presence in

the state. For example, in October 2008, the Indiana Tax Court held that an out-of-state credit card issuer is subject to the state's financial institutions tax, despite the fact that the company does not maintain any tangible property or employees in Indiana. The Indiana court cited the rationale of a similar decision issued by the Supreme Court of West Virginia. Many more states may now become emboldened to follow the leads of Indiana and West Virginia and press for taxation of the activities of out-of-state entities.

Thus far, the U.S. Supreme Court has declined the opportunity to settle the debate over whether mere economic presence in a state is sufficient to permit state taxation of business activities. Congress could clarify matters, and, in fact, multiple bills have been introduced in the U.S. House of Representatives that would prohibit state taxation of an out-of-state company unless the company has a physical presence in the taxing state. However, as of this writing, no such bill has emerged from the House Subcommittee on Commercial and Administrative Law, and the fate of the proposed legislation is unclear.

Given the uncertainty in this area, and the potential for tax liability in dozens of states across the country, companies doing business of any kind across state lines should obtain the services of a multistate tax professional to assist them in making an analysis of the company's methods of business and its tax exposure.

*—by David L. Chilcoat, a partner (retired) in the Columbus law firm of Campbell Hornbeck Chilcoat & Veatch. Updated by Jon Murphy, an associate with the Columbus law firm of Means, Bichimer, Burkholder & Baker Co., LPA.*

### **Business Taxes: Part of the Cost of Doing Business**

#### ***Q: I just started a new business in Ohio. What do I have to do about taxes?***

**A:** First, your business should file for its federal Employer Identification Number (EIN), commonly known as the tax identification number. Your business should have an EIN even if it has no employees. To obtain the number, complete Internal Revenue Service Form SS-4. Through the form, the IRS asks basic questions such as the business name and address, the names of the owners or officers, the form of business (for example, corporation, limited liability company, partnership or sole proprietorship), the starting date of the business, a brief description of the business, its accounting year end and the number of employees expected over the next year. Form SS-4 and other IRS forms and instructions may be obtained from the IRS Internet site, [www.irs.gov/](http://www.irs.gov/).

#### ***Q: What happens after I complete Form SS-4?***

**A:** You may complete and file Form SS-4 online through the IRS Internet site or you may telephone the information on the form to the IRS. By applying online or by telephone, you will receive the EIN immediately. Alternatively, you may apply for an EIN by facsimile or mail. The instructions for Form SS-4 contain the addresses and telephone numbers for filing the form. Whatever method is used, after the IRS processes the registration, the IRS will send your business the applicable federal income tax and payroll and withholding tax forms. Your business may still need to register with state and local authorities.

***Q: What about state and local registrations?***

**A:** If your business will have employees, it must file for employer identification numbers in the state and locality where the employees work. These filings will establish the business's accounts for state and local payroll and withholding taxes. In Ohio, unemployment compensation and workers' compensation also require registrations. In addition, certain types of businesses may need local licenses or permits before opening. Finally, if your business will collect and remit sales tax as a retailer, your business will need an Ohio vendor's license. You may obtain information and forms about Ohio taxes from the Ohio Department of Taxation at its Internet site, <http://tax.ohio.gov> or by mail from the Ohio Department of Taxation, P.O. Box 530, Columbus, Ohio 43216-0530. Ohio's state government Internet site has a section about registration and taxes for new businesses at <http://business.ohio.gov/starting>.

***Q: What taxes will my business pay?***

**A:** Essentially, your business could be taxed by three levels of government: 1) federal; 2) state; and 3) local. In addition, for income taxes, your business could be taxed at its location and anywhere it conducts business if its business activities establish some connection or nexus to other locations beyond sales solicitation. Business taxes and the concepts of nexus and solicitation are involved; therefore, no short, definitive answer is possible here. However, Ohio businesses typically will owe federal, state and local income taxes; federal, state and local payroll and withholding taxes; state and local sales or use taxes; and local real property taxes.

In addition, because some taxes depend upon the type of entity or the type of business conducted, other types of income, excise, property or transaction taxes could apply.

***Q: When will my business pay these taxes?***

**A:** Timely payment of taxes is required to avoid penalties and interest. Deadlines for filing some tax returns may be extended, but generally the time for payment of the tax

owed may not be extended without incurring interest charges.

For calendar-year corporations, federal income taxes are payable in estimated quarterly installments on March 15, June 15, September 15 and December 15. Local income taxes usually follow the federal quarterly schedule. For corporations doing business in Ohio, the Ohio franchise tax is due in three payments on January 31, March 31 and May 31. The Ohio franchise tax will be phased out in 2010.

Ohio has a commercial activity tax (CAT), a business gross receipts tax that replaces the Ohio corporation franchise tax and the Ohio personal property tax. Depending upon the amount of gross receipts, CAT filers file and pay the tax annually or quarterly.

For pass-through entities, such as partnerships, sole proprietorships and some limited liability companies, the owners pay the income taxes. For the owners of such passthrough entities who are persons, the personal income tax rules apply and both federal and Ohio income taxes are paid quarterly on April 15, June 15, September 15 and January 15. Local income taxes may be due on quarterly basis, too.

Federal, state and local payroll and withholding taxes are generally due monthly or semiweekly. After registration, tax authorities will give your business payroll and withholding tax payment schedules that will vary according to the estimated amount due. Real property taxes in Ohio are due twice a year. The due dates are December 31 and June 20, but most counties extend these dates.

### ***Q: When are the tax returns due?***

**A:** For calendar-year-end corporations, the federal corporate income tax return is due the March 15 following the year end. Local income tax returns may be due then too. For corporations, Ohio requires the corporation franchise tax return on January 31. For Ohio's commercial activity tax, annual filers file a return on February 9, and quarterly CAT filers file returns on May 10, August 9, November 9 and February 9.

For calendar-year-end partnerships, the federal partnership return is due March 15. For other pass-through entities, the personal income tax rules apply to owners who are persons, making April 15 the due date for reporting business income (or loss) on a personal income tax return. Local governments may require income tax returns on these dates too.

Ohio sales tax returns are due semi-annually, quarterly or monthly depending on the sales

tax due and whether the business holds a vendor's license or a direct pay permit. Federal, state and local payroll and withholding tax return due dates also vary depending upon the amount due.

Finally, the IRS, Ohio and most local governments require annual reconciliations of the prior year's payroll and withholding taxes by January 31. Also, the IRS requires businesses to provide employees and others certain information returns, such as Form W-2 or the Form 1099 series, by January 31.

Business and personal taxes are detailed and have many variables. Therefore, the information presented here considers only some basics. No general answer can cover all situations.

*—by Scott F. Sturges, an attorney with the Columbus office of McNamara and McNamara, LLP.*

### **Contact the Law Office of Michael J. Davis**

To talk to Michael J. Davis about your legal concerns, please contact us by calling 513-604-8391 or emailing us at [davislaw01@gmail.com](mailto:davislaw01@gmail.com)

Michael J. Davis is located in Mason, Ohio, and serves clients throughout Ohio, including Lebanon, Maineville, Mason, Morrow, Springboro, South Lebanon, West Chester, Warren County, Butler County, Hamilton County, Clermont County and Clinton County, Ohio.

