

Impact

An Overview of Current Legal Events of Concern and Interest

Fall 2005

Ohio's New Commercial Activity Tax — the CAT has Claws

By: Thomas C. Rink



In an effort to make Ohio more tax-friendly to manufacturing businesses, the General Assembly made major changes to Ohio's tax code effective on July 1, 2005. The changes affect most Ohio businesses and Ohio income taxpayers. The most visible change is the introduction of the Commercial Activity Tax ("CAT"), which is a tax on the privilege of doing business in Ohio measured by the gross receipts of the business. The CAT is being phased in over five years and replaces the Corporation Franchise Tax and the Tangible Personal Property Tax, which are being phased out over the same five-year period. Generally, Ohio-based manufacturers and retailers that have been paying significant tangible personal property and franchise taxes may see a tax reduction. Service companies, non-Ohio companies with significant sales in Ohio, and high-volume, low-margin businesses may see a tax increase. Also, Ohio personal income taxpayers will see their Ohio income tax rates cut by a total of 21% over the next five years.

Most enterprises doing business in Ohio will be subject to the CAT tax and are required to register and pay a one-time fee by November 15. There are exceptions for non-profit organizations, governmental agencies, financial institutions, insurance companies and similar businesses. *Taxpayers with less than \$150,000 in annual taxable gross receipts will not be subject to the new tax.* Sole proprietors, partnerships, LLCs, LLPs, C-corporations, S-corporations, and trusts are all potentially subject to the CAT. *A flat tax of \$150 applies to the first \$1 million of taxable gross receipts.* The tax rate of 0.26% applies to receipts over \$1 million, but because of the five-year phase-in, the effective rate is lower through March 31, 2009.

"Taxable gross receipts" are all receipts other than certain specifically excluded items, and there is no deduction for the cost of goods sold or other expenses. Thus, *businesses pay the CAT regardless of whether they operate at a profit.* A taxpayer must measure gross receipts using the same accounting method used for federal income tax purposes.

Some items are specifically excluded from the definition of gross receipts:

- interest income, except interest on credit sales
- dividend income and distributions received
- receipts from the sale of motor fuel, but only for the first 24 months of the CAT
- receipts from the sale, exchange or other disposition of an asset that is subject to capital gains treatment under the Internal Revenue Code (without regard to the length of time the asset has been held)
- distributive or proportionate shares of receipts and income from a pass-through entity

Only taxable receipts allocated to Ohio are subject to the tax. For example, gross rents and royalties from real property or tangible personal property located in Ohio or used in Ohio are allocated to Ohio. Similarly, gross receipts from the sale of real property located in Ohio will be allocated to Ohio, as well as gross receipts from the sale of tangible personal property received by the purchaser in Ohio. Gross receipts from the sale of services and most other receipts will be allocated to Ohio in the proportion that the purchaser's benefit in Ohio bears to the purchaser's benefit everywhere. This is not an all-inclusive list, but it should give you a flavor for the allocation rules.

Any person that has a substantial connection (nexus) to Ohio is subject to the CAT. The new law provides that "substantial nexus," for purposes of the CAT, means one of the following: the person owns or uses a part or all of its capital in Ohio; the person is qualified to do business in Ohio; the person has a "bright-line presence" in Ohio; or the person otherwise has nexus pursuant to the U.S. Constitution. "Bright-line presence" is defined to mean that a person has at least \$50,000 of property in Ohio; has at least \$50,000 of payroll in Ohio; has at least \$500,000 of sales in Ohio; has at least 25% of its total property payroll and sales in Ohio; or is domiciled in Ohio. There is some question about the constitutionality of the "bright-line" test, so stay tuned.

Every person or entity subject to the CAT **must register with the Tax Commissioner by November 15, 2005**, or within thirty (30) days after first becoming subject to CAT,

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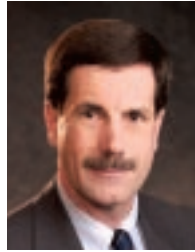
Super Lawyers are Plentiful at Strauss & Troy!

Should Your Company Have an Employment Manual?

By: Claudia G. Allen
and Paul B. Calico



Claudia G. Allen



Paul B. Calico

When employers call to ask whether they should have an employee policy manual (also called employee handbooks), we typically ask what prompted the question. Usually, such calls are the result of confusion about how to handle some aspect of the employer-employee relationship — either how to apply the company's existing policies to new facts or how to deal with a situation for which the company has no policy. Employers are rightfully concerned about having standard policies that provide fairness and consistency, while worrying about being tied to a set of rigid rules that allow little room for flexibility.

A policy manual does create valid employee expectations that the company will follow its policies, so it is important to be sure a particular company's policies are right for that company. It is sometimes tempting for companies to “borrow” a “canned” employee manual, such as one used by a manager's former employer. After all, if it worked for them, it should work for us, right? However, policy provisions that are appropriate or necessary in one environment may not be appropriate in others. Just as a tailored suit will fit better than one off the rack, a company's handbook should be tailored to fit its business.

Some standard provisions should find expression in every company's policy manual. All policy manuals should contain a language verifying the company's intention to comply with all state and federal employment laws. Such “Fair Employment Practices; Equal Employment Opportunity” provisions confirm that the company will not consider sex (gender), race, color, age, religion, nationality, or ancestry in making employment decisions. It is likewise important to have a policy that allows and encourages employees to report suspected instances of discrimination or harassment, thereby allowing the company to investigate and take appropriate action.

Not only do such provisions provide a good reminder of the company's legal obligations, they can also avoid potential liability. In a series of cases alleging corporate responsibility for sexual harassment, the United States Supreme Court has held that a company is not liable for harassment by a co-worker if (1) it had an effective procedure for victims to report discrimination or harassment and (2) the plaintiff/employee did not follow the procedure. In order for this “safe harbor” to apply, however, the courts have required companies to include provisions making it clear that they will not retaliate against employees who report discrimination or harassment.

Some companies have attempted to limit such anti-retaliation provisions to good-faith claims. It is important to note, however, that the Equal Employment Opportunity Commission views such limitations as implied threats of reprisal, which could have a “chilling effect” on employees. In other words, the EEOC is concerned that an employee who is unsure about reporting suspected conduct might be deterred from doing so if the company's handbook limits its protection to good-faith claims. As a result, it is the EEOC's position that companies with limited anti-retaliation provisions are not entitled to the safe harbor protection of an effective anti-discrimination and harassment policy.

To enjoy full protection, employers should avoid statements concerning good-faith or false claims and instead deal with any such situations as is appropriate in each case.

Another somewhat surprising limitation for employment manuals relates to confidentiality provisions. While it is appropriate and advisable to include policy provisions reminding employees to keep information about the company and its clients/customers confidential, the National Labor Relations Board recently held that such provisions go too far if they limit employee's rights to discuss the terms and conditions of their employment. What does this mean? The NLRB took the position that a handbook provision preventing employees from discussing their wages constituted an unfair labor practice since it had the effect of interfering with employees' rights to organize (as in union organization).

In deciding what else belongs in your policy manual, you might start by determining what is most important to your business. If your employees must be at their workstations ready to work at a precise time, your manual should make this requirement clear. (We also recommend that companies have accurate job descriptions stating the essential functions of each position.) If employees have the option of flex-time, allowing them to begin work between certain times and then to work eight hours, your manual should clarify the flex-time rules.

Implementing or revising an employment manual provides an excellent opportunity to regulate issues that may have been too fluid or inconsistent in the past. For example, you can set the company's policy about how vacation time is granted, when personal days are paid, when lunch hours may be taken, what is appropriate office attire, and whether the Internet can be used for personal purposes. For employees, knowing what the rules are can eliminate confusion and tension.

Most importantly, nothing in the manual should be contrary to your company's actual practices. If you do not give quarterly reviews, don't say that you will. If you list conduct that merits discipline, you are implicitly excluding other behaviors. Progressive discipline may not be appropriate in all situations: if you require two written warnings before you can fire someone, you may be saddled with a bad employee until he makes yet another mistake. If you provide progressive discipline to one employee, you are required to provide progressive discipline to other employees who engage in the same conduct. Otherwise, you may be subjecting the company to a claim of discriminatory treatment. This is really just another way of saying that the policies and procedures must be applied fairly and consistently.

Finally, your manual should make it clear that the company reserves the right to change its policies. You should periodically review the manual to see if the policies still meet the company's needs. We suggest that employers use a loose leaf-binder so new policies and replacement pages (dated as of the effective date of the change) can be added. All employees should sign an acknowledgement that they received the manual and all changes. Those records should be kept in employee personnel files, verifying that they are aware of the company's expectations and commitments.

Ms. Allen and Mr. Calico regularly practice in the area of Employment Law, including the preparation and revision of Employment Manuals.

Attorneys on the Move



Claudia G. Allen

Claudia Allen and **Paul Calico** will speak at the 2005 Northern Kentucky Law Review Symposium on Employment Law Ethics. The symposium attracts employment lawyers from a multi-state area and features noted national and local employment law professors and practitioners who will speak on a variety of timely issues. Ms. Allen will speak about *Ethical Issues Relating to Employee Benefits*; Mr. Calico will speak on the *Ethics of Client Counseling in Employment Law*.



Paul B. Calico

Jeremy A. Hayden spoke at a recent Cincinnati Bar Association seminar on *Corporate Formation: Advising Closely Held Businesses*.

James G. Heldman has been appointed Co-Chairman of the Major Gifts Division of the Jewish Federation's 2006 Campaign.



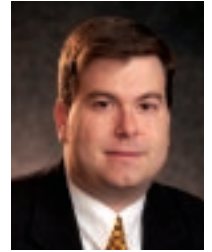
Jeremy A. Hayden



James G. Heldman

Joseph J. Braun, **Matthew R. Chasar**, and **Jason D. Tonne** will coach two St. Xavier High School Mock Trial teams again this year. One of the St. X teams, coached by Joe Braun, advanced to the State competition last year. Jason Tonne also serves on the Cincinnati Bar Association Young Lawyer Section Continuing Legal Education Committee, which organized the 2005-2006 CBA No Brown Bag Series, which consists of 19 seminars on various legal topics.

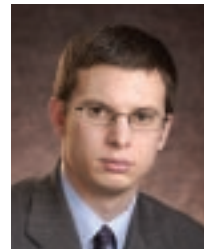
R. Guy Taft serves as Treasurer and is on the Board of Trustees of the **Cincinnati Bar Foundation**, which supports programs to promote justice, educate the community about the law, improve the quality and administration of justice in the community, support the delivery of legal services to all, and foster professionalism and civility in the practice of law. **Richard S. Wayne** and **Joseph J. Braun** lead the firm's fundraising for the Foundation. We are proud of the fact that 100% of the attorneys at Strauss & Troy support the Cincinnati Bar Foundation and contribute annually to its general fund.



Joseph J. Braun



Matthew R. Chasar



Jason D. Tonne



R. Guy Taft



Richard S. Wayne

Our Community— Our Commitment

SPONSORSHIPS

As a part of our tradition of sharing our gifts and talents with others, Strauss & Troy is pleased to have sponsored an array of deserving causes over the past few months. We are proud to have supported the following programs and events in fulfillment of our continuing commitment to give back to the Greater Cincinnati community:

- American Bar Association Annual Fall Conference
- Beechwood Athletics Boosters
- Beechwood Education Foundation
- Childrens Dental Care Foundation
- Cincinnati Cardinals Baseball
- Cincinnati Childrens Choir
- The Cincinnati Herald
- Cincinnati Opera
- Cincinnati Preservation Association
- Cincinnati USA Regional Chamber
- Covington Rotary Club
- Falmouth Rotary
- The Friends of SPCA
- Healing Connections Association, Inc.
- Hopewalk
- Jewish Vocational Services
- The John P. March III Memorial Golf Event
- Kids Helping Kids
- Milford United Methodist Church
- Northern Kentucky University
- Southland Hall Association
- Village of Lincoln Heights

Client Spotlight



Infintech (Innovative Financial Technologies), a Cincinnati-based company with sales presence throughout the United States, offers consultative payment processing solutions, product technologies, and services to merchants, banks, associations, and franchises in nearly every one of our nation's industries. In today's rapidly growing "cashless society," Infintech helps business owners take control of their payment processing expenses by helping them understand, compare and implement new payment technologies with a trusted payment partner.

Accepting Credit Cards Can Be a Profit-Generator.

Numerous social, demographic and technological factors combine to make plastic the payment form of choice for increasing numbers of people. Accepting credit cards is becoming a must for all businesses big and small in today's economic environment.

The Evolving Industry. Consumers are using credit cards in increasingly more purchase environments: online, fast food, doctor's offices, law firms and just about anywhere an economic exchange can take place.

- The average American cardholder has an estimated 4 credit cards
- Credit card usage has increased 15% each year over the past 5 years (3 times faster than the increase in overall U.S. purchases)
- Debit/Bankcard purchases are growing at 50% each year
- Credit/Debit cards are expected to account for 48% of all purchases by next year (60% by 2007)
- Increasingly, businesses now use purchasing cards and commercial cards to buy products/services

Embracing the Evolution. Businesses that accept credit cards have a competitive advantage against businesses that do not accept them. As these industry trends continue, businesses not accepting credit cards in the past will need to do so in the future, and businesses that do currently accept credit cards need to pay close attention to the costs associated with acceptance.

Making the Decision. Deciding to take credit cards and with whom to process them are significant business decisions. The key is to work with a trusted company that has a proven track record of service, loyalty and experience. This is where Infintech has differentiated itself from other processors.

The Benefits of a Trusted Partner. Infintech is led by a management team with over 25 years' experience in the payment processing industry. Infintech was founded on the principle that most business owners do not have a complete understanding of the costs they pay to accept credit cards. The reality is, most business owners simply do not have the time to track and worry about these costs until they start compiling exorbitant expenses that could have been avoided. Unless you are an expert on payment processing, it has become nearly impossible to understand all the costs and interchange rates Visa and MasterCard pass through.

Infintech's mission is to provide innovative payment services and products to their clients, enabling them to be more competitive and profitable in their respective markets. Their success hinges on vision, passion, knowledge and experience within the merchant processing industry. Infintech has recently been recognized as the preferred merchant service provider for the Cincinnati Bar

- Complimentary Analysis & Consultation on current processing rates
 - Affordable and modern equipment solutions
 - Internet & Mobile payment solutions
 - Electronic check services
 - Gift & Rewards programs
 - 24/7 Live customer support
 - No application fees, conversion fees, reprogramming fees or hidden costs
- Association and the Cincinnati Dental Society, and has been featured in the *Cincinnati Business Courier*. Infintech has established a proven reputation for combining trusted service, security and savings.

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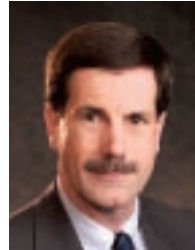
Super Lawyers are Plentiful at Strauss & Troy

Ten Strauss & Troy attorneys have been selected as *Ohio Super Lawyers for 2006*. Over 35,000 Ohio attorneys cast votes for the best lawyers they had personally observed in action, and a panel reviewed and ranked the nominees in over 50 practice areas. The attorneys in the top 5% were then designated as Ohio Super Lawyers. We are pleased to announce Strauss & Troy's 2006 Super Lawyers:

Claudia G. Allen
Charles G. Atkins
Paul B. Calico
Ann W. Gerwin
James G. Heldman

Thomas C. Rink
Thomas L. Stachler
William V. Strauss
R. Guy Taft
Richard S. Wayne

Paul B. Calico, Marilyn J. Maag, and Thomas L. Stachler have also been selected for inclusion in the 2006 edition of *The Best Lawyers in America*®. Selection as a *Best Lawyer* is considered a singular honor, and is based on an exhaustive peer-review survey in which attorneys throughout the country confidentially rate the legal abilities of their professional peers in their areas of specialty. Fewer than 1% of the attorneys in the United States achieve this distinction.



Paul B. Calico



Marilyn J. Maag



Thomas L. Stachler

Buy-Sell Agreements for Closely Held Entities

By: William V. Strauss

Parties who are forming a closely held corporation, limited liability company ("LLC"), or limited partnership should think in advance about how they will get out of the venture if there is a breakdown in the circumstances of the business or essential aspects of the parties' relationship. Parties to new ventures are naturally optimistic about their prospects and assume that they will continue to get along well during the lifetime of their relationship. It becomes the lawyer's obligation to intrude into this blissful scene and politely suggest that even those who are unfazed by danger — astronauts for example — should have an exit strategy, both for the end of the mission and in the event of an emergency.



A buy-sell agreement is a contractual arrangement among the owners of a business, outlining methods to save the venture from the almost certain destruction of value that will occur if there are major unanticipated events such as the death of an owner, the desire of one owner to sell his interest to another, or a major disagreement among the owners. The parties should give some thought as to what types of disagreement are sufficiently serious to trigger the emergency exit provisions. In the event of such a disagreement, the parties should consider a specified "cooling off" and discussion period, possibly even the mandated use of a neutral third party (e.g. a mediator), prior to severing of their relationship. However, if that effort fails, the otherwise frozen members need an emergency exit to avoid adverse consequences, such as a court-ordered dissolution followed by a forced sale of the company's assets. The buy-sell agreement, then, is the emergency exit that provides predictability and continuity of ownership, and creates a market for the owners' interests. For an LLC, the buy-sell agreement is usually included in the company's operating agreement.

There are generally two possible purchasers in a buy-sell agreement, the remaining owner(s) or the business entity itself. When the remaining owner(s) purchase the selling owner's interest, it is typically pursuant to a "cross-purchase" buy-sell plan. Alternatively, when the business entity purchases the seller's interest, the buy-sell is usually pursuant to a "stock redemption"

procedure. Each method has its unique advantages and disadvantages, and the proper choice depends on the type of business and the individuals involved. In either case, the most common methods for arriving at a purchase price are: book value (easy to compute, but probably not reflective of market value); the formula approach (typically a multiple of earnings or net income); agreed value (owners agree to initial value and then update annually); and appraised value (probably the most accurate, although appraisals can be costly).

In many situations where one owner exits, there are complexities regarding third-party participants, the most important of which is probably the entity's lender. The parties should consider whether the sale of an ownership interest would constitute a loan default. The selling owner may also be a guarantor on the firm's debt. Is it possible for the departing party to be released from the guaranty and at what cost? The parties also should be cognizant of any other agreements that prohibit a change in ownership or control; the provisions of a major lease might be one example.

Finally, a successful buy-sell outcome may be dependent upon the remaining owners' ability to purchase the selling owner's interest. This could be accomplished by installment payments, a lump sum payment, or a combination of the two. However, the parties should contemplate the possibility that the remaining owner(s) will be unable to fund the purchase. Accordingly, it may be desirable to include a fallback provision in which the departing owner is given the right to sell to an outside party. In that case the remaining owner should have a meaningful right of first refusal to match the terms of a contemplated sale to a third party, and possibly a "tag along" right to opt into the sale and avoid being left out of a favorable deal.

As can be seen from the above discussion, the buy-sell agreement is an important document for closely held entities. The terms of the agreement should be tailored to meet the needs of the particular venture and the owners involved. A thoughtful and well-drafted agreement entered into at the beginning of a venture can provide a predictable and equitable method for resolving future disagreements, if and when they arise, and prevent or minimize the loss of value that would otherwise result.

Bill Strauss is president of Strauss & Troy.

Ohio's New Commercial Activity Tax — the CAT has Claws *continued*

if later. Registration must be made on a form provided by the Commissioner and must include identifying and other information specified in the statute or otherwise required by the Commissioner. A one time \$15 registration fee is payable for electronic registration; paper registration requires a fee of \$20. Fees are credited towards the first tax payment due. In addition to the individual business, the CAT rules contemplate two different types of taxpayer groups: a consolidated elected taxpayer based on an election; and a combined taxpayer, which is in effect an involuntary default category for non-electing taxpayers under common control. *If you are possibly in a consolidated elected group or combined group of taxpayers, you should carefully study the impact of being included in one of these groupings.* There may be major differences.

This article is not designed to be a full explanation of CAT. We hope merely to draw your attention to the fact that the CAT has been adopted, that registration is required, and that if you are in a group of entities that may possibly be consolidated or combined, you should carefully consider whether to elect the consolidated elected taxpayer status. Once you have registered and paid the registration fee, you will not have to file your first tax return until February 10, 2006 for the initial return period covering July 1, 2005 through December 31, 2005. You will have to pay at least \$150 privilege tax for the calendar year 2006 by May 10, 2006. Subsequent returns are due on a quarterly basis if the taxpayer is expected to have receipts over \$1 million in a year; otherwise returns are due annually on February 10. A tax return will be sent to all registered taxpayers before the first return is due.

If you have questions concerning the CAT, please contact Tom Rink, the head of Strauss & Troy's Tax Department.

*The rules of the Supreme Court of Kentucky require the following statement in any material of this type: "THIS IS AN ADVERTISEMENT."
If you wish additional or more specific information, please contact one of the attorneys at Strauss & Troy.*

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