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Avoid Tax Penalties by Correcting Employment, Severance and Deferred Compensation Arrangements in 2010

by: [Joel Farrar](#)

Nonqualified deferred compensation arrangements are required to comply, in writing, with the highly technical rules of Internal Revenue Code Section 409A ("Section 409A") effective as of January 1, 2009. A "deferred compensation arrangement" is any arrangement with an employee or independent contractor that could result in compensation being paid in a year following the year in which the compensation is earned. Thus, the term may include traditional deferred compensation plans, as well as employment agreements, independent contractor agreements, bonus arrangements, severance plans, stock incentive plans and management service contracts.

Failure to comply with the rules of Section 409A could result in the employee having to recognize all amounts "deferred" under the arrangement as current income, plus interest and a 20% penalty. The employer could also be subject to penalties and interest for not withholding sufficient income and employment taxes.

The IRS recently published guidance that permits an employer to correct a Section 409A failure in the document that sets forth the terms of the arrangement. The IRS previously published guidance that permits an employer to correct a failure to comply with Section 409A in the operation of an otherwise compliant plan. Corrections made during 2010 avoid significant penalties. After 2010, the correction procedure will continue to be available but penalties may apply.

We recommend that all employers have their deferred compensation arrangements, including employment agreements, independent contractor agreements, bonus arrangements, etc., reviewed for compliance with Section 409A during 2010, so that any errors might qualify for penalty-free correction.

If you have any questions regarding this tax benefit, please contact:

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Michigan Defense MBT Credit

by: [Jean Shtokal](#) and [Nicholas Oertel](#)

Qualifying Michigan companies may be eligible for a refundable tax credit against the Michigan Business Tax (“MBT”). In 2008, Michigan enacted the Defense Contracting MBT Credit (“Defense MBT Credit”) in hopes of helping Michigan companies secure contracts with the Department of Defense, Department of Energy, and the Department of Homeland Security. The Michigan Economic Growth Authority (“MEGA”) determines whether to award a Defense MBT Credit.

For a company to qualify for a Defense MBT Credit, the company must satisfy the following requirements:

1. Create a minimum of 25 Qualified New Jobs;
2. Win a federal contract with the Department of Defense, Department of Energy, or Department of Homeland Security;

3. Maintain the number of full-time jobs it had prior to securing the contract;
4. Ensure that its employees work a minimum of 35 hours per week.

If a company qualifies for the Defense MBT Credit, MEGA determines the amount and duration of the credit.

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IT Tip Corner

Software Licenses Do Not Automatically Transfer in a Merger or Acquisition

by: [Samuel Frederick](#)

Software licenses provide businesses with the right to use software programs. Many of these programs become interwoven into the fabric and function of the company. As a general rule, companies do not own the software that they license. The corollary is that they then do not, unless expressly agreed, possess the right to transfer or assign the licensed software they use to a new entity when later involved in a merger, acquisition or internal corporate restructuring.

In Cincom Systems, Inc v Novelis Corp., 581 F.3d 431 (6th Cir. Sept 2009), the Sixth Circuit Court of Appeals affirmed a \$460,000.00 intellectual property infringement claim in favor of a software licensor against a business for attempting to transfer its software license to a new company created by a merger.

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Federal common law provides that copyright licenses (read software licenses) are unassignable absent express language to the contrary. Therefore, a merger, acquisition or corporate restructuring may constitute an impermissible transfer of an intellectual property license absent text in the license agreement to the contrary.

If your company is considering a merger, acquisition or internal corporate restructuring, it is important that intellectual property contracts (such as software licenses) be carefully reviewed to determine if the

merger may have an effect on the surviving company's ability to use the software or other intellectual property. As a matter of course, companies should review new software agreements to ensure that the agreements provide for a "transferable" license. Many boilerplate software agreements do not.

If you have any questions regarding software licenses in a merger or acquisition, please contact:

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Carry-Back Net Operating Losses and Save

by: [Timothy Burkhard](#)

Recent tax law changes expand opportunities to use net operating losses. The Worker, Homeownership, and Business Assistance Act of 2009 allows businesses that had a net operating loss in 2008 or 2009 to use those losses to recoup taxes paid in the prior five years. Under prior law, such losses could be carried back only two years.

There are, however, limitations on this tax benefit. Subject to certain exceptions, such an election may be made for only one tax year. Additionally, a net

operating loss carried back to the fifth year before the loss year is generally limited to 50% of the available taxable income for that year and certain other limitations apply.

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The HIRE Act May Save Your Tax Dollars

by: [Joel Farrar](#)

The recently enacted Hiring Incentives to Restore Employment (HIRE) Act may benefit your business with tax savings. The Act creates the following tax opportunities.

- **Employment Tax Exemption.** The HIRE Act exempts employers from paying the 6.2% employer Social Security tax on wages paid in

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- 2010 to newly hired workers who were previously unemployed, but only if the newly hired workers do not replace other employees of the employer and certain other requirements are met.
- **Tax Credit for Hiring.** Employers will receive up to a \$1,000 tax credit for each previously unemployed worker that the employer hires after February 3, 2010 and employs for at least 52 consecutive weeks, but only if the employee's wages during the final 26 weeks of the period are at least 80% of her wages for the first 26 weeks of the period and certain other requirements are met.
- **Enhanced Expensing.** Small business taxpayers may elect to write-off the cost of certain capital

expenses in the year of acquisition in lieu of depreciating the property over time. The American Recovery and Reinvestment Act of 2009 and a prior law in 2008 had increased the maximum amount that can be expensed in 2009 and 2008, respectively, to \$250,000, and had also increased the phase-out threshold for 2009 and 2008 to \$800,000. The Hire Act extends these increases to 2010, offering potential tax savings to small businesses that make qualifying investments in 2010.

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