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Commentator **Vol. 24, Issue 4**

As we go to press, much remains unsettled with respect to the fiscal cliff and our taxation system from January 2013 forward. Hopefully, by the time you receive this edition of the *Commentator*, Congress and the Administration will have found a compromise solution that takes the country off the fiscal precipice and provides a method of taxation that allows both businesses and individual taxpayers to plan for the future.

In this issue, tax-related articles discuss pass through entities being attacked by the IRS for paying business owners unreasonably low compensation and how to prepare for the full impact of the Affordable Care Act.

Non-tax articles relate to the Foreign Corrupt Practices Act, which is an attempt to prevent corruption, and Michigan's new Right-to-Work legislation.

Finally, we say farewell and best wishes to former Kemp Klein attorneys Allen Zemmol (who retired in December) and Debra Nance, who is now participating in "judges school" and will be sworn in as a District Court Judge next month.

Best Wishes,

IRS hot button issue

Attacking S Corporations for paying unreasonably low wages

Ralph A. Castelli, Jr.

Historically, one of the reasons C Corporations were converted to S Corporations dealt with situations where the shareholder/employees were being paid such substantial salary and bonus compensation that there was a fear the IRS could successfully attack the compensation as being unreasonably high (allowing the IRS to disallow a portion of the compensation deduction by recharacterizing part of the payments as dividends). This then would result in double tax (the imposition of corporate tax, and then individual tax to the shareholder/employee recipient).

With the substantial increase in the Social Security wage base over the last several years, coupled with the imposition of the Medicare tax which is not subject to any wage base limitation, many owners of S Corporations preferred to take S Corporation distributions, rather than substantial salaries. This has led the IRS to attack the salaries of shareholder/employees as being unreasonably low.

On October 1, 2012, the U.S. Supreme Court declined to review a decision of the Eighth Circuit Court of Appeals which held that an S Corporation paying unreasonably low salary was liable for employment taxes on dividends which were reclassified as salary. The Eighth Circuit decision affirmed the decision of a district court, which found that the shareholder/employee's $24,000 salary in 2002 and 2003 was unreasonably low. It allowed the IRS to reclassify over $67,000 in dividend payments for each year as salary to the shareholder/employee during those years. This resulted in the corporation owing employment taxes on the reclassified dividend payments.

The Eighth Circuit did note that while the reasonable compensation issue normally comes up in determining whether a business is attempting to deduct too high an amount of compensation, the IRS has found the concept equally applicable to employment tax cases.

For further information regarding these matters, please contact Mr. Castelli at ralph.castelli@kkue.com or 248.740.5668.

In this Issue:

Seminars

February 25, 2013
Medicaid Update 2013

Brian R. Jenney will speak at The National Business Institute's **Medicaid Update 2013**. The seminar will be held Monday, February 25, 9:00 a.m.-4:30 p.m., at Embassy Suites Hotel Detroit-Southfield, 28100 Franklin Road, Southfield, MI. Mr. Jenney's topics will be ***The Medicaid Application Process*** and ***Medicaid Estate Recovery***. For more information or to register, go to www.nbi-sems.com.

May 9–11 (Acme, MI) & June 14–15 (Plymouth, MI), 2013
53rd Annual Probate and Estate Planning Institute

Joseph P. Buttiglieri will be a presenter and moderator at The Institute of Continuing Legal Education's oldest and most popular program. Mr. Buttiglieri's topic will be ***Appointment of the Personal Representative***.

These all day seminars will be held on:

- Thursday, May 9 - Saturday, May 11, at the Grand Traverse Resort & Spa, 100 Grand Traverse Village Boulevard, Acme, MI; and
- Friday, June 14 - Saturday, June 15, at The Inn at St. John's, 44045 Five Mile Road, Plymouth, MI.

To register for either seminar, go online to www.icle.org or call 877.229.4350.

Prepare now for federal health care

Thomas L. Boyer and Kevin J. McGiness

On March 23, 2010 President Obama signed into law the Patient Protection and Affordable Care Act (PPACA) commonly referred to as Obamacare, the Affordable Care Act and the Federal Health Care Law. The statute is over 2,000 pages long and there are very few explanatory regulations or "official interpretations." The Act is very detailed, complicated and in some cases contradictory. Much of the complexity is the result of the law's need-based approach in that there are few concrete numbers, but rather formulas governing the application of PPACA to individuals and their dependents based upon income and other economic factors.

Some aspects of the law such as maintaining children on their parents' insurance until age 26, the proscription of benefit maximums and no denial of coverage due to pre-existing conditions are currently in effect. The requirement for employers to furnish coverage to their employees is effective January 1, 2014. However, the extent of employee coverage depends upon the number of employees in 2013 and the number of hours worked by those employees in 2013. Therefore, to avoid an unpleasant surprise on New Year's Day 2014, employers must review their employee demographics in detail to determine whether adjustments in the workforce are needed to predict the employer's health care coverage obligations in 2014.

The Affordable Care Act requires large employers to either offer health insurance to their full-time employees or pay a penalty through the Internal Revenue Service. A full-time employee is defined as an employee who averages 30 or more hours per week. A large employer is one that averages 50 or more full-time employees and full-time equivalent employees (FTEs).

To determine if an employer is a large employer necessitates determining the number of employees averaging at least 30 hours a week in 2013 and adding to that figure the number of FTEs. The number of FTEs an employer has is based upon taking the aggregate monthly hours worked by part-time employees (those who work fewer than 30 hours per week) counted on a monthly basis during calendar year 2013, divided by 120.

If an employer is a large employer resulting from the formula which is outlined above, it must provide minimum essential health care coverage going forward to all employees who average at least 30 hours a week during a previous period which can vary between 3 and 12 months during 2013. Minimum essential coverage is subject to a number of criteria. The amount an employee may pay as a share of the premium is based upon the employee's W-2 income.

As you can see from this basic overview, the PPACA is extraordinarily complex. The point of this article is that even though compulsory health care coverage and/or the related fines do not begin until January 1, 2014, whether you are subject to this law as a large employer and which of your employees are entitled to the medical coverage is a result of your employment activity in 2013. Several measures can be taken to regulate whether you will be deemed a large employer in 2014 and which of your employees are entitled to medical coverage, but those measures need to be taken now.

For further information regarding these matters, please contact Mr. Boyer at t.boyer@kkue.com or 248.740.5666; and Mr. McGiness at kevin.mcginess@kkue.com or 248.740.5685.

Foreign Corrupt Practices Act

Bribery is illegal even if it is customary local practice in some countries.

Stuart Sinai

Of course you are aware that bribing any federal, state or local government official or any employee of a government agency is a crime. Are you equally aware, however, that bribing an official or an employee of a foreign government (or even a government-owned or controlled separate entity) can be a crime in the U.S. regardless of the laws of that country and where the bribe was paid? Furthermore, the Foreign Corrupt Practices Act (FCPA) applies to both publicly-traded and private U.S. companies as well as to U.S. citizens.

What is the definition of a "bribe" under the Act?

What might be considered as just following local practice in some countries can be considered a "bribe" under the FCPA It includes, of course, straight out cash payments. However, it also includes "anything of value." One luncheon is not likely a violation but numerous meals could be when the seeming purpose is to influence conduct to obtain or retain business or to merely gain a competitive advantage or balance. Gifts, indirect payments to a relative or a business controlled by the official, advances or reimbursement for travel or other "expenses" or offering to pay or provide any type of benefit, can be considered illegal.

When operating in certain parts of the world, it is customary to hire advisors and consultants. Payments to them in excess of what is necessary to pay for reasonably comparable services may be an indication that a portion of the "fees" are actually intended to be used to bribe and influence someone in government important to your objectives. To attempt to alleviate the possibility that your company would be tainted by the consultant's misuse of his fees, we urge that all agreements with the foreign consultant require that it abide by all U.S. laws, including specifically the FCPA. Those agreements can also include indemnification provisions requiring reimbursement for any costs, expenses or fines the client suffers as a result of the consultant's violations. Needless to say, actually collecting from a Russian or Chinese foreign consultant is more a dream than a reality. Accordingly, the best you can do is to check out the reputation of those who you hire and demand an accounting of every dollar paid to any third party.

Every company should have an anti-corruption policy/program in place especially if business is conducted in any foreign environment where doing business is rife with those who have been accustomed to payoffs. We can help you craft a policy that will help your employees know what is a normal business expense versus a possible illegal payment or expenditure and how to handle unlawful requests. Executives of U.S. firms can face both cash fines and criminal charges for acts of employees and agents that occur here or in foreign countries. Implementing anti-bribery controls and adopting written policies can provide an essential mitigating defense to Justice Department allegations of complicity.

For further information regarding these matters, please contact Mr. Sinai at stuart.sinai@kkue.com or 248.740.5660.

Firm News

Kemp Klein attorneys in *DBusiness* 2013 list of Top Lawyers

Kemp Klein attorneys **William B. Acker**, **Irwin M. Alterman**, **Joseph P. Buttiglieri**, **Alan A. May**, **Stuart Sinai**, **Amy A. Stawski** and **Thomas V. Trainer** have all been selected by a vote of their peers to be included in *DBusiness* magazine's list of 2013 Top Lawyers to appear in the November/December 2012 issue of *DBusiness* and online at *www.dbusiness.com*.

Weikert interviewed for Auto Retail News & Insight

Michael J. Weikert spoke with AutoRetailNet publisher Edmund Chew about why so few dealership buy/sells are being done this year. The interview appeared in the October 5 issue of AutoRetailNet's online industry newsletter.

Trainer receives 2012 Call to Justice Award

Thomas V. Trainer is a recipient of the ***2012 Call to Justice Award*** sponsored by Elder Law of Michigan to honor his advocacy for the rights of older adults and people with disabilities.

Commentator now available electronically

If you would like to receive our quarterly newsletter via email instead of snail mail, please call Gayle Roberson at 248.528.1111, x611 to provide your email address for this purpose.

Michigan's new Right-to-Work Amendment

Thomas L. Boyer

On December 11, 2012, the Michigan legislature passed and Governor Snyder signed an Amendment to the 1939 statute which established the Michigan Employment Relations Commission. This Amendment established Michigan as the 24th Right-to-Work state.

Previously, Michigan was referred to as a Union Shop state. In virtually every collective bargaining agreement in Michigan there is language that states that to retain employment by a unionized employer an employee must join the union within 31 days and pay all fees and dues or pay a service charge, which is approximately the same amount as union dues. If an employee does not satisfy this requirement, the union can compel the employer to fire him or her.

The new Right-to-Work Amendment states in pertinent part:

> "An individual shall not be required as a consideration of obtaining or continuing employment to do any of the following: … (B) Become or remain a member of a labor organization. (C) Pay any dues, fees, assessments or other charges or expenses of any kind or amount…to a labor organization."

Therefore, even if a union is the exclusive bargaining agent of a group of employees, the employees cannot be compelled to be members of the union or pay dues or assessments to the union to avoid termination.

Since a labor organization represents and bargains for the entire bargaining unit, unions view right-to-work legislation as creating a class of workers who refuse to pay dues or a service charge to the union yet take advantage of the benefits provided by the union contract. Additionally, right-to-work opponents point out that wages are lower in right-to-work states.

Supporters of right-to-work legislation argue that such legislation promotes business activity and increases employment. Indiana became a right-to-work state in February, 2012 and claims to have been quite successful in attracting new business. Cause and effect has not yet, however, been proven. But, the fact that the Japanese car companies, Boeing and a high percentage of all new large manufacturing plants are located in right-to-work states is probably not a coincidence.

Regardless of one's viewpoint on this legislation, it is obvious that the landscape has dramatically changed.

It is important to note that the Michigan Right-to-Work Amendment is effective with the next collective bargaining agreement between the employer and the union. Therefore, if a union contract does not expire until December 31, 2015, nothing changes until then.

For further information regarding these matters, please contact Mr. Boyer at t.boyer@kkue.com or 248.740.5666.

Kemp Klein Law Firm would like to wish all of you a safe, happy and prosperous New Year in 2013.