2018
CRITICAL LEGAL DEVELOPMENTS

VisTaTech Center, Livonia, Michigan

October 31, 2018

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Agenda

8:30 - 8:40	Opening Remarks	
8:40 - 9:10	Estate Planning - Key Concerns in 2018	Lisa J. Walters
9:10 - 9:40	Basics of Estate and Trust Administration	Monica D. Moons
9:40 - 10:20	The Anatomy of an Asset Sale Transaction	Christopher M. Williams
10:20 - 10:50	Break	
10:50 - 11:20	Key Commercial Real Estate Purchase Agreement Provisions Demystified	Ronn S. Nadis
11:20 - 12:00	Choice of Entity Strategies as They Relate to the New Tax Law	Gary Schwarcz
12:00 - 12:30	Avoiding Discrimination and Harassment in the Workplace - A Guide for Small Employers	David A. Lawrence

This material does not attempt to give specific legal or tax advice. For advice in particular situations, the services of competent legal, tax or financial planning advisors should be obtained.

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GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF INSURANCE AND FINANCIAL SERVICES
LANSING

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One credit is 50 minutes of instruction with no more than 10 minutes for a break. Fractional credits will not be awarded. Registration, coffee and lunch breaks, or social hours do not qualify for CE credit.

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Estate Planning - Key Concerns in 2018

Lisa J. Walters

ESTATE PLANNING - KEY LAWS, DEVELOPMENTS AND PLANNING OPTIONS

I. OVERVIEW OF APPLICABLE TAXES

A. Key estate and gift tax rules.

1. Lifetime/death exemption.

a. $11,180,000 in 2018, increasing to $11,400,000 in 2019. IRC Section 2010(c).

b. File Form 706 for taxable estates, to make a QTIP election or for portability election. Portability preserves deceased spousal unused exclusion amount.

2. Annual gifting exclusion.

a. $15,000, plus unlimited amounts paid directly to the providers for medical expenses and tuition - 2018 and 2019.

b. For gifts to a non-citizen spouse - $152,000 in 2018; $155,000 in 2019.

c. File 709 for future interest gifts, gifts in trust, or gifts over the annual exclusion.

3. In planning, count all assets, consider appreciation and consider alternate valuation.

4. Provide beneficiaries with Form 8971 Sch. A basis information. IRC 1014(f).

a. File with IRS within 30 days after estate tax return is filed.

b. Not required if 706 is filed only for portability or to allocate GST.

c. Recipient must use Schedule A values for basis.

d. Monetary penalties apply for failure to file; penalty for omitted items is $0 basis.

e. Estate tax value and income tax value must be the same.

f. Use higher value and elect portability?

g. No regulations to date.

B. Key income tax rules.

1. Applicable highest ordinary income tax brackets for 2018.

a. Individuals - 37% over $500,000 + 3.8% Medicare Tax.

b. Joint filers - 37% over $600,000 + 3.8% Medicare Tax.

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c. Trusts - 37% over $12,500 + 3.8% Medicare Tax.

d. Capital gain - 20% + 3.8% Medicare Tax.

2. For 2019, the taxable income levels at which the maximum rates will apply will be adjusted for cost of living increases, using a new "chained" index. The estimated brackets, courtesy of www.forbes.com, are:

   a. Individuals - 37% over $510,300 + 3.8% Medicare Tax.

   b. Joint filers - 37% over $612,350 + 3.8% Medicare Tax.

   c. Trusts - 37% over $12,750 + 3.8% Medicare Tax.

   d. Capital gain - 20% + 3.8% Medicare Tax.

C. New Developments.

1. Focus on basis.

   a. Allocating all assets to a Residuary/Credit Shelter Trust results in basis step up only on first death.

   b. A Joint Trust yields a 50% step up in basis on first death and a 100% step up in basis on second death. However a trust which divides into a Marital Trust/Credit Shelter Trust may only get 1 step up.

   c. Alternative Structure - 100% to marital (outright or QTIP) with spouse having the option to disclaim to a Residuary/Credit Shelter Trust. Elect portability. Portability can protect both lifetime estate tax exclusions. Step up in basis at the first spouse's death and again at the second spouse's death when the assets are treated as part of the survivor's estate.

2. Estate of Duane Francis Horton II, Michigan Court of Appeals No. 339737 (July 17, 2018). In Horton the Michigan Court of Appeals concluded that a typed document existing only in electronic form on the decedent's phone, having his full name typed at the end of the document, was a valid Will. The decedent had left an undated, handwritten, journal entry in his own handwriting stating "my final note, my farewell is on my phone." The Court relied on MCL 700.2502 and the formalities of a holographic Will were not required. Extrinsic evidence was permitted to show the decedent's intent.

3. Sveen v. Melin, 138 S. Ct. 1815 (2018). In this decision, the Supreme Court held that a Minnesota statute providing that the dissolution of a marriage automatically revoked a prior life insurance beneficiary designation naming the divorced spouse was valid and applicable. This case confirms the importance of keeping beneficiary designations up to date.

4. Millstein v. Millstein, et al., 2018-Ohio-1204 (Court of Appeals of Ohio, No. 106270 March 29, 2018). In Millstein, the Ohio Court of Appeals held that the creator of an Irrevocable Trust did not have standing to seek reimbursement from

the trust of millions of dollars of income taxes he paid on trust income under the grantor trust rules. The case illustrates the importance of carefully monitoring Irrevocable Trusts, carefully complying with the applicable tax compliance and reporting rules and timely addressing issues that arise.

5. PLR 138069-17, 201840007 (October 5, 2018) provides a detailed discussion of the rules applicable to stretch out over the lifetime of the oldest child of the payment of a decedent's qualified plan account to Discretionary Trusts for his children. This favorable ruling rests in part on the beneficiaries' limitation of their power of appointment at death only to individuals younger than the oldest child. PLR 110889-18, 201831004 (April 30, 2018) favorably rules that the surviving wife could roll over and stretch out an IRA payable to a Joint Trust on her husband's death. See also PLR 201736018 (June 9, 2017). Although PLRs may not be relied on by other taxpayers, the IRS analysis is instructive.

6. An issue of increasing importance is the nexus required by a trust with a State before that State may tax trust income. Residence of the beneficiary or settlor is a critical, but not controlling factor. See Blue v. MI Department of Treasury, 185 Mich. App. 406 (1990); Kaestner Trust v. NC Department of Revenue, NC Supreme Court No. 307PA15-2 (June 8, 2018); Fielding v. MN Department of Revenue, MN Supreme Court No. A17-1177 (July 18, 2018). Additional legislation and litigation may be expected. Advisors should be cautious.

7. In Gordon v. Fishman, FL D. Court of Appeal, No. 2D17-1488 (August 24, 2018), the court concluded that a Will signed before the decedent was married was not automatically voided upon later marriage and divorce to the beneficiary named. This decision was reached in spite of a statute providing that upon divorce a Will is to be construed as if the former spouse had predeceased the decedent. The case emphasizes the importance of regularly updating estate planning documents, particularly after a divorce or other major family event occurs.

8. Numerous other decisions and rulings impact planning for clients in applicable situations, such as reforming trusts to preserve Grantor Trust status, the timeliness of disclaimers, and extensions of time to allocate GST exemptions, make estate distributions, use alternate valuation or elect special use valuation.

II. THE NEW NORMAL - JOINT TRUSTS?

A. Overview.

1. Living Revocable Trust preferred, commonly a Joint Trust.

2. Pour-over Will.

3. Financial Durable Power of Attorney.

4. Patient Advocate Designation and Living Will.

5. HIPAA Authorization.

6. Funeral Representative Designation.

7. Funding.

B. Joint Trusts - considerations.

1. Simplicity - like joint ownership in operation and at death.

    a. Similar to joint ownership.

    b. Provides property management in case of disability without lifetime Probate.

    c. May avoid Probate at death on funded assets.

    d. Handles disposition of assets at death.

    e. Beneficiaries still have the option of using disclaimers for potential estate tax planning.

        (1) See IRC Sections 2046 and 2518.

        (2) See MCL 700.2901.

    f. May be drafted to create a separate trust at the first death (Equalizing Trusts), although this is not typical since some or all of the step up in basis may be lost with this arrangement.

    g. Subject to claims of creditors.

2. Basis step up.

    a. 50% first death, subject to proof that the decedent contributed more than 50%, and 100% at second death. IRC Sections 1014(a), (b)(9), (e).

    b. Basis increase is limited to adjusted basis at time of original gift when gifted to decedent within 1 year of death when inherited by original donor.

3. Lost control?

    a. Either spouse can access assets during lifetime.

    b. Must both parties consent to amendments?

    c. May either party revoke or must both act together?

    d. Should trust be irrevocable at first death?

4. No creditor protection for the survivor.

5. No tenancy by the entireties creditor protection.

    a. Available for real estate, bonds, stock owned as tenants by the entireties. MCL 554.45, 557.51.

    b. May be available for brokerage accounts. Shapiro v. Nicoloff, No 01-CV-71591-DT, 2001 U.S.D. LEXIS 26298 (ED Mich. Sept. 25, 2001).

    c. Not available for bank accounts.

6. No outside management with surviving spouse in control. Is assistance needed?

7. Potential loss of first lifetime exclusion, absent a portability election.

8. Some non-testamentary transfers may still be appropriate to avoid Probate.

    a. Wills are subject to Probate and Testamentary Trusts may be subject to Probate.

    b. Contractual beneficiary designations and "pay on death" provisions may lack detail, successors.

    c. Joint ownership with children may be risky depending on child's situation.

    d. A trust provides management in case of disability of creator and/or beneficiary.

C. Multiple trusts - considerations.

1. Asset protection maximized.

    a. Assets can be insulated from beneficiary's creditors.

    b. Assets can be insulated from beneficiary's new spouse.

    c. Assets can be excluded if the survivor seeks government assistance, provided proper discretionary provisions are included.

    d. Separate ownership of business or inherited property can occur.

    e. Allows use of two generation skipping transfer exemptions

2. Allows separate or non-family trustees and trust protectors.

3. Allows retaining ongoing control over asset disposition.

4. Add flexibility with powers of appointment, trustee removal powers, trust protectors.

5. Step up in basis and availability of lifetime exemptions depend on funding formulas.

    a. Funding Residuary Trust first results in step up in basis only at first death, uses estate tax exemption.

    b. Funding Marital Trust first results in step up in basis at first and again at second death, but uses only the surviving spouse's estate tax exemption.

    c. A 100% QTIP Marital Trust funded first can maximize control. QTIP election must be made on a 706. 100% step up in basis at second death.

    d. A 100% Marital Trust with control by the surviving spouse with a possible disclaimer is flexible.

6. Must use with Qualified Domestic Trust situations involving a non-citizen spouse.

D. Funding - considerations.

1. Which assets are protected from creditors, probate or taxation?

2. Which spouse is more "at risk"?

3. Which assets need a basis step up?

4. Which assets need an income tax stretch out?

5. Which assets should pass outside of the trust?

6. Which assets should be used to fund charitable gifts?

7. Insurance has a key role to play - asset protection and creation; liquidity.

E. Supporting documents - considerations.

1. Who should be in charge - Personal Representative; Guardians; Trustee; medical decisions; funeral arrangements; financial power of attorney?

2. When should documents be effective?

3. Patient Advocate Designations (PAD) and HIPAA waivers.

4. Funeral Representative Designation.

5. Is documentation up to date and complete?

6. Do adult children have proper documentation, especially Patient Advocate Designations, HIPAA authorizations and Durable Powers of Attorney?

F. Advanced estate planning still has a place.

1. Taxable estates.

a. Multiple Marital/Residuary Trusts.

b. Lifetime gifting, including leveraged and trust arrangements.

c. Irrevocable Life Insurance Trusts.

d. Form 706 Estate Tax Return elections.

2. Special Purpose Trusts.

a. Domestic Asset Protection Trusts.

b. Discretionary Trusts.

c. Pet Trusts.

d. Gun Trusts.

e. Other.

3. Special cases.

a. Fixing Irrevocable Trusts.

b. Charitable gifting, including private foundations.

c. Assets in foreign jurisdictions.

d. Other.

III. APPLYING WHAT WE KNOW

Personalizing estate planning documents is becoming increasingly important. As the estate tax applies to fewer and fewer people, the emphasis has shifted to dealing with special circumstances, concerns and problems involving heirs, and income tax planning. "Boilerplate" language or "canned" documents are inadequate. Other family members, friends, business associates and others all have unique circumstances and documentation may vary.

A. Asset protection and detailed distribution standards - creditors; spendthrifts; minors.

1. During settlor's lifetime.

a. Adequate insurance is essential, with an umbrella policy.

b. Emphasize exempt qualified plan assets.

c. Note protected ownership of Michigan real estate by husband and wife.

d. Transfer assets to less risky spouse?

e. Consider LLC and family limited partnership structures for risky assets.

f. Use corporate and LLC structure for businesses.

g. Investigate Domestic Asset Protection Trusts.

h. A Living Trust does not shelter assets from the settlor's creditors, but can shelter assets from the spouse's and other beneficiary's creditors.

2. At the first spouse's death.

   a. Is this a second marriage?

   b. Is remarriage a concern?

   c. Can the survivor manage assets/money?

   d. Do children need funds? What is their relationship with the survivor?

   e. Should gifts to non-immediate family be limited to a percentage of the estate? Note that a percentage calculation requires a full accounting to prove how the percentage amount was calculated and may not be possible until administration is otherwise complete.

   f. Should powers of appointment be included?

3. At the surviving spouse's death.

   a. Do children need protection from a spouse or a creditor?

   b. Are children minors?

   c. Are children spendthrifts?

   d. Is generation skipping a goal?

   e. Do children have "special needs" considerations?

   f. Should beneficiaries be treated differently - advances, education, lifetime gifts?

   g. Do beneficiaries need protection of their government benefits?

B. Tax minimization - estate; income.

   1. Minimize income and rates.

   2. Defer or delay.

   3. Permit distribution of income to charity.

C. Privacy - Probate avoidance; minimizing disclosure.

1. Probate applies to personally owned assets, with special exceptions:

    a. Joint assets - consider control and basis issues.

    b. POD assets - consider intended payout restrictions and successor beneficiaries.

    c. Assets with a beneficiary designation.

    d. Assets owned by Living Trusts.

2. Qualified plan assets may need special trust wording to ensure maximum tax stretch out.

3. Even trusts have notice and disclosure to beneficiary rules. MCL 700.7814.

D. Retaining flexibility.

1. Consider distributions based on clear standards.

    a. Health.

    b. Education (define carefully).

    c. Maintaining standard of living.

    d. Support - food, clothing, shelter, transportation.

    e. Consider "other resources" or not? Specify.

2. Consider special standards.

    a. Study abroad.

    b. Buying a home.

    c. Funding a business.

    d. Paying for a wedding or funeral.

    e. Supporting dependents.

    f. Restrict distributions with specified undesirable behavior?

    g. Contestability clauses?

    h. Cannot avoid certain creditors of a beneficiary without purely discretionary trust provisions - child support, alimony, IRS and state taxes.

    i. Purely discretionary distributions?

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3. Consider detailed powers of appointment.
4. Consider trust protectors.
5. Consider requiring consultation with trusted investment advisors.
6. Consider powers to remove or change trustees.
7. Consider disclaimers.
8. Require child have a Prenuptial Agreement?
9. Require child to have an estate plan in place?

E. Estate planning mistakes commonly observed.

1. Having inadequate liquid assets - Use insurance as needed.
2. Inappropriate distribution provisions for the surviving spouse.
    a. Outright versus QTIP?
    b. Which marital formula is desired?
    c. Pay IRAs outright versus in trust?
    d. Include other heirs in the Residuary?
    e. Include available flexibility in the Residuary?
3. Failure to protect heirs from creditors/mismanagement.
4. Failure to simplify with a Joint Trust when appropriate.
5. Failure to fund trusts.
6. Inappropriate IRA beneficiary designations.
7. Inappropriate funding formulas for Residuary/Credit Shelter Trusts.
8. Using joint ownership to transfer assets or to avoid Probate.
9. Using or preparing deeds without proper advice.
10. Failing to address the distribution of personal property.
11. Failing to provide for charitable gifts.
12. Failing to provide for "final takers".
13. Failing to provide flexibility in documents.

14. Failing to have all needed documents.
15. Failing to update documents.
16. Failing to leverage the use of the lifetime exclusion during life if appropriate.
17. Failing to consider generation skipping provisions if appropriate.
18. Improper operation of Irrevocable Life Insurance Trusts.
19. Failure to provide for family business succession.

Basics of Estate and Trust Administration

Monica D. Moons

BASICS OF ESTATE AND TRUST ADMINISTRATION

I. INTRODUCTION

A. Methods for Distributing Assets on Death.

1. Joint ownership.

2. Contract, i.e. beneficiary designation.

3. Ladybird or similar deeds.

4. Living or Revocable Trust.

B. Assets pass through the "probate process" if they were owned in the Decedent's sole name and do not pass through one of the other methods listed above. Testamentary Trusts that are created in the decedent's Will are subject to probate.

C. The extent of Probate Court involvement, if any, depends on the nature of the assets involved, the manner in which the assets were owned and the cooperativeness of the parties.

II. KEY WORDS AND CONCEPTS

A. "Ancillary Administration" is the procedure for authorizing a personal representative who has been appointed in Michigan, to take action with respect to assets of the decedent, which may be located outside Michigan. Assets such as real estate outside of Michigan can involve probate here and where located.

B. "Application" versus "Petition". An Application (PC 558) is the Probate Court form used to initiate informal proceedings in Probate Court. The Probate Court Register decides whether to grant the relief requested in an Application. A Petition (PC 559) is used to initiate formal proceedings in Probate Court. A Probate Court Judge decides whether to grant the relief requested in a Petition. Formal proceedings are typically used when an estate is complex or may involve disagreements among the parties.

C. "Probate Property" or "Probate Estate". These two phrases mean the same thing. A person has probate property (or a probate estate) if, at the time of their death, they own assets that will not pass through any other arrangement (joint property, contract, trust, etc.) and will be subject to probate administration. The person or entity in charge of handling the probate proceeding is the "Personal Representative", formerly known as an executor. The "Trustee" is the person or institution in charge of a trust.

D. "Testate" v "Intestate". A person dies "testate" if they leave a valid Will. If they did not leave a valid Will, they died "intestate". When people die intestate, if they have "probate property," that property will pass according to the statutes stating the rules of "intestate succession."

III. GENERAL CONCEPTS IN ESTATE AND TRUST ADMINISTRATION

A. Types of Trusts.

1. “Revocable Trusts” v “Irrevocable Trusts”.

2. “Inter Vivos Trusts” or “Living Trusts” v “Testamentary Trusts”.

B. Types of People.

1. “Current Trust Beneficiary” v “Qualified Trust Beneficiary”.

2. “Interested Persons”.

C. Allowances and Elective Shares.

1. “Allowances”.

2. “Elective Share” or “Forced Share”.

D. Michigan Law Governing Estate and Trust Administration.

1. The Estates and Protected Individuals Code (“EPIC”).

2. The Michigan Trust Code (MTC).

E. Notice Requirements.

1. Probate Estate. In the administration of a probate estate, the personal representative has a variety of notice requirements established by law and court rule.

2. Trust Estate. In the administration of an inter vivos revocable trust, the trustee has similar duties to provide information.

F. Publication for Creditors and Handling Claims.

G. Record Keeping.

1. Inventory.

2. Accounting.

3. Time records.

H. Tax Returns.

1. Income tax returns.

2. Estate tax return.

I. Fees.

1. Fiduciary and agents.

2. Attorney.

3. CPA.

IV. DISTRIBUTING ASSETS AND CLOSING THE ESTATE OR TRUST

A. Probate Estate.

1. Distribution of assets.

2. Closing the estate.

B. Trust Estate.

1. Distribution of assets or establishment of subtrusts.

2. Terminating the trust.

V. CONCLUSION

The devil is in the details in estate and trust administration. It is essential for a fiduciary to keep meticulous records and to keep the interested persons or trust beneficiaries informed throughout the process. A fiduciary who follows those two cardinal rules will simplify the administration process and will also fare better, if the administration ends up in court upon the objection of an interested person or trust beneficiary.

The Anatomy of an Asset Sale Transaction

Christopher M. Williams

THE ANATOMY OF AN ASSET SALE TRANSACTION

I. SCOPE OF PRESENTATION

A. Asset Sale Transaction: A transaction in which some or all of the assets of a business are sold.

B. Asset transactions involving substantially all of the assets of the business. Effectively, a sale of the "business," but not the business entity.

C. Assets: All tangible and intangible interests owned by a Seller business (e.g. equipment, inventory, intellectual property, goodwill, cash, accounts, deposits, records, etc.).

D. Michigan legal considerations.

E. Seller and Buyer perspectives.

II. SESSION GOALS

A. To understand the process of completing an asset sale transaction from beginning to end.

B. To identify "value add" opportunities for professionals assisting in an asset sale transaction.

III. PRE-PLANNING

A. Extremely important for Sellers to engage in pre-planning before entering into negotiations to sell business assets.

B. Pre-planning should happen years in advance; not immediately prior to a sales negotiation.

C. Key Pre-Planning Activities.

1. Evaluating goals and objectives.

a. Financial considerations.

b. Timing considerations.

c. Buyer considerations.

(1) Family.

(2) Management.

(3) Third-party.

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2. Evaluating and supporting the value of your business.

   a. Value the business.

   b. Is there a gap between the owner's perceived value and what can be supported?

   c. Review and evaluate financial statements.

      (1) Consider from a Quality of Earnings perspective (i.e. a report that makes normalizing adjustments to reported EBITDA - Earnings before interest, taxes, depreciation and amortization).

      (2) Consider from a Net Working Capital perspective (i.e. current assets minus current liabilities).

      (3) Financial statements need to show the company's financials trending in the right direction. The 6 month window before closing is critical.

3. Keep reliable books and records.

4. Customer and contract considerations.

   a. Assignability of contracts and permits.

   b. Approved vendor considerations.

5. Key tax considerations.

   a. What is the tax impact of an asset sale transaction?

   b. Does the Seller's entity structure maximize tax advantages?

6. Key employee considerations.

   a. Who would a Buyer want to retain?

   b. How will Seller retain key employees in anticipation of a sale?

   c. Are employees subject to confidentiality, non-solicitation, and non-competition agreements?

D. Sellers will <u>not</u> maximize their value if their house isn't in order.

   1. Buyers will be spooked and pay less or cancel the deal if problem areas are identified and can't be adequately explained or quickly resolved.

   2. Transaction costs will be higher as expedited professional services will be required to meet transaction deadlines.

E. There are many opportunities for professional advisors to assist in this process.

1. Ask questions: What is your plan?

2. Assist in the pre-planning process.

3. Connect clients with qualified professionals.

4. Professional advisors help clients by identifying any biases and blind spots.

IV. PRELIMINARY TRANSACTION MATTERS

A. Source of Offers.

1. Directly from third-party buyers.

a. Strategic buyers.

(1) Make us better.

(2) Make them better.

b. Financial buyers.

(1) Investment.

(2) What is their experience in the business?

(3) How long will they be around?

2. Management.

a. How will they pay?

b. Employee vs owner mentality.

3. Family.

4. Investment bankers and business brokers.

a. Service contract.

b. Scope of services.

c. Fees.

(1) Monthly fees.

(2) Success fees.

(3) How are fees calculated and when are they paid?

B. Non-disclosure agreements and other restrictive covenants.

1. Sellers should have a non-disclosure agreement in place before disclosing sensitive or proprietary information to prospective Buyers.

2. Depending on the circumstances, it may be necessary to have additional restrictive covenants in place.

   a. Non-solicitation agreements with respect to employees prevent a Buyer from attempting to hire Seller employees.

   b. Non-solicitation agreements with respect to vendors, suppliers, and/or customers prevent a Buyer from attempting to form a business relationship with Seller vendor, suppliers, and customers.

   c. Non-competition agreements prevent a Buyer from competing with a Seller.

C. Letter of Intent.

1. A letter of intent provides an overview of general transaction terms a Seller and a Buyer have agreed to prior to entering into definitive transaction documents.

2. A letter of intent sets the ground rules for negotiation and provides a framework for the definitive transaction documents.

3. From the Buyer's perspective, the letter of intent should include a "no shop provision" to prevent a Seller from negotiating with other potential Buyers.

4. From the Seller's perspective, transaction leverage can shift to the Buyer the longer the transaction is pending. Accordingly, it is important to have a clearly defined closing timetable.

5. Generally, the letter of intent should be non-binding except for certain key provisions which may survive a terminated letter of intent (e.g. confidentiality provisions, divisions of expenses, "no shop" provisions, etc.).

6. Higher end deals may include a break-up fee if a party terminates the letter of intent without a contractually permissible reason.

V. PRE-CLOSING MATTERS

A. Due Diligence.

1. Due diligence is the process by which a Buyer studies a Seller's business and a Seller confirms a Buyer's ability to complete a transaction.

2. Areas that a Buyer should examine include:

   a. Existence, title to, liens upon, and condition of assets.

   b. Uniform Commercial Code (UCC) searches.

c. Financial statements (both audited and unaudited).

d. Accounts receivable and accounts payable reports.

e. State and federal tax returns.

f. Contracts (both written and verbal), warranties, permits, and licenses.

g. Real property, including title, encumbrances, zoning, condition, and environmental matters.

h. Intellectual property, including copyrights, trademarks, patents, and domain names.

i. Insurance policies and claim information.

j. Litigation and claims including litigation searches.

k. Labor and employment matters.

l. Benefit plans and arrangements.

m. Seller organizational documents and minute books.

3. Areas that a Seller should examine include:

a. Buyer organizational documents.

b. Litigation and claims including litigation searches.

4. Professional advisors should assist and coordinate in the due diligence process.

B. Pre-Closing Notices, Filings, and Forms.

1. UIA 1027 - Business Transferor's Notice to Transferee of Unemployment Tax Liability and Rate.

a. The purpose of this notice is to notify the Buyer of the Seller's unemployment tax rate and payment history as, generally, a Buyer who acquires 75% or more of the assets of a business is liable for unemployment taxes and interest owed as of the date of transfer, up to the reasonable value of the organization, trade, business, or assets acquired less the Buyer's security interest in the assets.

b. Under Michigan law, the Seller must provide the Buyer with the form at least two calendar days (not counting Saturdays, Sundays, or legal holidays) before the Buyer accepts the Seller's offer to transfer the business (i.e. signs the purchase agreement).

c. Failure to provide accurate information on the UIA 1027 is a misdemeanor that may result in imprisonment of up to 90 days, a fine of up to $2,500, and a consequential damages award.

d. Contact the Unemployment Insurance Agency ("UIA") to obtain Form UIA 1346 - Disclosure of Transferor Account - to accurately complete the UIA 1027.

2. UIA 1395 - Clearance of Account.

   a. This form certifies the status of taxes owing the UIA by the Seller.

   b. A party should request the UIA 1395 at least 10 days prior to the closing.

   c. When the UIA provides the UIA 1395, which certifies Seller's tax liability to the UIA as of the request date, the Buyer will not be liable for any amount due from the Seller in excess of the amount certified by the UIA.

   d. Buyer may want to hold back part of the purchase price or have a portion of the purchase price held in escrow until another UIA 1395 showing no outstanding tax liability can be obtained post-closing.

3. Michigan Department of Treasury Form 5156 - Request for Tax Clearance Application.

   a. Under Michigan law, a Buyer of a going or closed business or its stock of goods is required to escrow funds to cover the Seller's unpaid taxes, interest, and penalties until the Seller produces a receipt from the state treasurer or the state treasurer's designated representative that the taxes have been paid or a certificate that no taxes are due and owing.

   b. Upon the Seller's written waiver of confidentiality, the Michigan Department of Treasury shall within 60 days of receipt of the request, release to a Buyer the Seller's known or estimated tax liability for purposes of establishing an escrow account for the payment of taxes. This waiver and request is made by filing Form 5156.

   c. If the Buyer complies with the above provisions, Buyer will not be liable for Seller's unpaid taxes in excess of the amount escrowed. Furthermore, if the Michigan Department of Treasury fails to produce the known or estimated tax liability within 60 days of the receipt of the request, then the Buyer shall have no liability for Seller's unpaid taxes.

4. Other Notices.

   a. Worker Adjustment and Retraining Notification (WARN) Act notices, 29 USC Sections 2100, et seq.

   b. Hart-Scott-Rodino Antitrust Improvements Act of 1976, Pub. L. 94-435, 11 USC Section 18a.

   c. Notices to unions or employees.

d. COBRA notices.

e. Notices to customers and suppliers.

VI. KEY TERMS AND CONDITIONS OF THE TRANSACTION

A. Purchase Price and Payment.

1. Entire amount paid.

2. Portion paid.

    a. Down payment.

    b. Promissory note with interest.

    c. Collateral for repayment.

3. Adjustments to purchase price.

    a. Inventory adjustments.

    b. Accounts receivable adjustments.

    c. Net working capital adjustments.

    d. Earnouts.

4. Allocation of purchase price for tax purposes (IRS Form 8594).

B. Included and Excluded Assets.

1. All assets included less specific excluded items.

2. Only certain assets are included and everything else is excluded.

3. Common excluded assets can include:

    a. Cash and cash equivalents.

    b. Bank accounts.

    c. Insurance policies.

    d. Prepaid deposits.

    e. Corporate minute books and records.

    f. Tax returns, refunds, and credits.

    g. Vehicles.

C. Assumed and Excluded Liabilities.

1. Most common: Only certain liabilities are included and everything else is excluded.

2. Less common: All liabilities included except for specific excluded liabilities.

3. Identify assumed liabilities.

D. Consents and Liens.

1. Approval of third-parties.

   a. Are any contracts, licenses, or permits to be assigned?

   b. Assignment provisions and processes should be reviewed.

2. Discharge of liens.

   a. UCC terminations.

   b. Payoff letters.

E. Employment Matters.

1. Termination of employees by Seller.

2. Hiring of employees and/or consultants by Buyer.

   a. Employment agreements.

   b. Consulting agreements.

3. Employee benefit plans.

F. Real Estate Matters.

1. Leases.

   a. Termination with new lease.

   b. Assignment and assumption of lease.

   c. Proration of rent.

   d. Security deposit.

2. Purchase of real estate.

3. Environmental matters.

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G. Representations and Warranties.

1. Who is making them?

    a. Owners.

    b. Entity.

2. Scope.

3. Knowledge.

4. Survival periods.

    a. Forever.

    b. Expiration of statute of limitation.

    c. Specific time period (e.g. 12 - 36 months).

5. Fraud.

6. Representation and warranty insurance.

H. Indemnification.

1. Scope.

    a. Representations and warranties.

    b. Covenants.

    c. Line item indemnities. Watch out for double dipping!

2. Cap.

3. Basket.

    a. Deductible.

    b. Tipping.

4. Escrows and holdbacks.

5. Right to offset.

6. Sandbagging.

7. Materiality scrape.

I. Timing of Closing.

1. Sign and delay.
2. Sign and close.

J. Industry Specific Issues (Examples).

1. Transfer of patient records.
2. Government contracts.

VII. KEY TRANSACTION DOCUMENTS

A. Purchase Agreement.

1. The most important document.
2. One size does not fit all.
3. Needs to be reviewed from both a Seller's perspective and a Buyer's perspective.
4. Drafter has the advantage.
5. Needs to be reviewed by professional advisors.

B. Disclosure Schedules.

1. Attached to the Purchase Agreement.
2. Provides qualifications and exceptions to representations and warranties.
3. Needs to be accurate and complete to avoid liability.
4. A key area where professional advisors can help.

C. Financing and Security Documents.

1. Promissory note.
2. Security agreement.
3. UCC financing statements.
4. Personal guaranty.
5. Collateral assignment of life insurance.

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D. Closing Statement.

1. Wire instructions.

2. Payoff letters.

3. Professional advisor fees and commissions.

E. Ancillary Documents.

1. Bill of Sale.

2. Vehicle titles endorsed for transfer.

3. Assignment and assumption agreement.

4. Escrow agreement.

5. Employment agreements / consulting agreements.

6. Confidentiality, non-solicitation, and non-competition agreements.

7. Bring-down certificates.

8. Secretary's certificates for entity parties.

9. Corporate resolutions for entity parties.

10. Resignations.

11. Certificate of good standing for entity parties.

12. Amendment to articles to change name, if acquired.

13. Termination of assumed names / Certificate of assumed name.

14. Real estate acquisition documents.

15. Lease assignments / terminations.

VIII. CLOSING MATTERS

A. Satisfaction of Conditions Precedent.

B. Authorization and Approvals.

C. Insurance Matters.

1. Seller: What insurance should be adjusted?

2. Buyer: Is insurance in place?

D. Banking Matters.

1. Ensure all bank financing and loan documents are prepared.

2. Remove terminated employees from bank accounts being retained.

3. New signature cards will be needed for bank accounts being transferred.

E. Employment Matters.

1. Notice to employees.

2. Benefit plans and payroll in place for new employees.

F. Real Estate Matters.

1. Change of utilities.

2. Transfer keys, codes, combinations, and garage door openers.

3. Ensure all real estate documents are prepared if real estate is included.

IX. <u>POST-CLOSING MATTERS</u>

A. Post-Closing Adjustments to the Purchase Price.

1. Follow necessary procedures.

2. Pay attention to deadlines.

B. Post-Closing Covenants (Examples).

1. Access to records.

2. Retention of records.

3. Mail.

4. Litigation assistance.

C. Tax Filings.

1. Michigan Department of Treasury Form 5156 - Request for Tax Clearance Application.

2. Michigan Department of Treasury Form 163 - Notice of Change or Discontinuance.

3. IRS Form 8594 - Asset Acquisition Statement under IRC Section 1060.

4. UIA Schedule B - Successorship Questionnaire. To be completed by a Buyer.

5. Form UIA 1772 - Discontinuance or Transfer of Payroll or Assets in Whole or Part. To be completed by Seller.

D. Announcements.

E. Industry Specific Filings (Examples).

1. Statutorily required notice concerning sale of a medical or dental practice.

2. Statutorily required notice concerning transfer of patient records.

Key Commercial Real Estate Purchase Agreement Provisions Demystified

Ronn S. Nadis

COMMERCIAL REAL ESTATE PURCHASE AGREEMENTS DEMYSTIFIED

I. INTRODUCTION

Every commercial real estate transaction is different and there is no way to effectively create a form of Purchase Agreement that works for every deal. Using a standard form invariably fails to advance the interests of your client and a thorough review of a proposed purchase agreement by experienced professionals is virtually always beneficial. Each provision can be written to benefit either purchaser or seller. Although impossible to identify every possible issue or agreement term involved in a commercial real estate purchase agreement, these materials will highlight the most significant of the issues that should be considered in evaluating a commercial real estate purchase agreement. Following are some preliminary considerations:

A. Financial Consultant's Role in Analyzing or Creating a Commercial Real Estate Purchase Agreement -- Often financial and tax consultants can be important resources in helping the buyer or seller understand tax consequences and net income potential of real estate transactions.

B. Attorney's Role in Analyzing and/or Drafting a Commercial Real Estate Purchase Agreement -- Experienced legal counsel assists buyers and sellers in understanding and advocating for respective positions.

C. Types of Commercial Real Estate -- There are key differences in evaluating industrial, retail, multi-family or office.

D. Recognizing Seller vs Buyer Perspective -- Can't Negotiate on Both Sides. You should assume that a draft Purchase Agreement is tilted toward one side or the other depending upon the drafter. It almost always should be negotiated from your client's perspective.

II. IDENTIFYING INFORMATION - THE BASICS

Basic contract law requires that an agreement for the purchase/sale of real property be in writing, signed by the parties and contain all material terms. In addition to price and terms for payment (discussed below), basic information such as the names of the parties and a description of the property being sold should always be part of the agreement but surprisingly, are sometimes left out. Here are some considerations regarding these basic terms:

A. Commercial real estate purchases are fundamentally different from residential real estate purchases and the forms of purchase agreements are not interchangeable.

B. Be careful relying solely on the realtor/broker for the purchase agreement. Purchasers and sellers often rely on real estate brokers, particularly in residential transactions. Brokers perform an import role and their forms are typically adequate for a residential transaction. They often fall far short when they attempt to draft commercial real estate purchase agreements.

C. Some form purchase agreements identify only one or neither of the parties in the opening paragraph, leaving the parties to fill in names of the parties on the signature

line. This has resulted in numerous problems if the deal blows up when trying to identify the defaulting party.

D. Identifying a purchaser as an individual on "behalf of an entity to be formed", is not uncommon. What does that mean? Is the individual liable? Be sure purchaser has unfettered right to assign to an entity and be released from liability. Seller will require personal liability from the individual purchaser until the purchaser's entity assumes liabilities and only if there is significant earnest money deposit.

E. Insert proper contact information. This becomes especially important for notice purposes.

F. Proper description of property is fundamental. Failure to supply the legal description or other clear identification of property can create misunderstandings about what is being sold, if not contract enforceability issues. For example, in retail shopping center sales, outlots that appear to be part of shopping center may be owned by others and not be part of the sale.

III. DEAL TERMS

A. Earnest Money Deposit.

1. What is typical/appropriate amount for earnest money deposit ("EMD")? Seller wants enough to compensate for having property off market and enough to make it painful for purchaser to back out. All of this is particularly important if seller is relying solely on earnest money deposit for its recourse,

2. EMD is typically refundable during due diligence period. Purchasers want a "free look see" before committing "hard" money.

3. EMD is typically non-refundable after due diligence period. Once due diligence period has run, deposit should be non-refundable in the absence of a seller default.

4. Seller might consider requiring additional earnest deposit upon expiration of due diligence period.

5. Who holds Earnest Money Deposit? Typically, title insurance company/escrow agent hold escrows. This creates fairest arrangement if there is a dispute over recovery of the deposit. Sometimes parties or their attorneys hold the deposit. This often doesn't go well for one of the parties.

B. Price and Terms.

1. Purchase price and terms of payment are fundamental and must be included. Obtaining a mortgage to finance the purchase is often required by the purchaser. Unlike most residential transactions, financing is often not a separate contingency. From seller's perspective, it simply wants cash at closing wherever its source. Purchaser's due diligence typically runs in parallel with the lender's due diligence. Purchaser determines if the property passes muster for the lender during the due diligence period and if not, agreement is terminated.

2. If the sale will be seller financed, then the specific terms of the financing should be in the Purchase Agreement. Best practice is to attach the form of seller financing vehicle (e.g., Land Contract or Mortgage) seller will use at closing. Note that a land contract is a financing vehicle not a substitute for a purchase agreement.

IV. PURCHASER'S DUE DILIGENCE

Perhaps the most important provisions for a purchaser are the rights under the Purchase Agreement to conduct a proper and thorough due diligence investigation of the property. In a seller's market, due diligence periods are often squeezed so that neither purchaser nor its lender have sufficient time to complete them. Care should be taken to allow sufficient time to complete the basics. The following are the key areas of due diligence that should be covered in the agreement.

A. Title.

1. Requirement for title insurance guaranteeing marketable title subject only to matters of record (easements, building and use restrictions, etc.) and the lien for real property taxes not yet due or payable.

2. Purchaser should require that the standard exceptions be deleted. It is important to protect purchaser from liens, boundary conflicts such as encroachments or property lost through adverse possession.

3. Purchaser should review survey in connection with title review.

4. Premium for base policy is typically paid by seller.

5. Time period for review of title should commence from receipt of all exception documents and, if possible, from receipt of survey.

6. Purchaser should review all title exception documents to confirm that there are no unacceptable restrictions on the use of the property or hidden financial obligations. Review of easements often requires reference to a survey.

B. Survey.

1. Purchaser should require existing survey as part of seller's deliverables.

2. Be sure due diligence period allows time to obtain new survey, or recertification of existing survey. Survey should be reviewed in connection with title review.

3. Understand limitations of a "mortgage" or "boundary" survey and the benefits of obtaining an "ALTA" survey.

4. Purchaser typically pays for new survey or recertification of existing survey.

C. Environmental.

1. Michigan has favorable environmental laws; purchasers should take advantage of them.

2. Assure sufficient time to complete environmental investigation as needed (Phase I Assessment; Phase II Assessment; Baseline Environmental Assessment; Due Care Obligations).

3. Purchaser should require prior environmental report as part of seller's deliverables.

4. Seller may attempt to restrict invasive investigation and/or reporting to State of Michigan.

5. Purchaser should request copies of purchaser's environmental investigation reports if deal does not close.

6. Purchaser typically pays for investigations but adverse environmental conditions often result in negotiation regarding cost of mitigation and or due care obligations.

7. Purchaser typically indemnifies seller against property damage or personal injury associated with purchaser's environmental investigation.

D. Property Condition Evaluation.

1. Purchaser should evaluate condition of roof, HVAC, parking lot pavement and other potential deferred maintenance.

2. Consider re-negotiating purchase price based on newly discovered deferred maintenance.

E. Zoning and Building and Use Restrictions.

1. These are often overlooked, especially building and use restrictions. Be sure contemplated use of property is allowed. Some commercial properties that back to residential subdivisions are burdened with restrictions against commercial activity. Affirmative title insurance coverage or other steps are necessary.

2. Consider anti-competition restrictions from former owners and tenants.

F. Access Rights - Need for Easement.

1. Be sure that property allows for access from a public street. If no access, then is easement provided? Purchaser should obtain affirmative coverage over any necessary beneficial easements.

2. Access to certain properties can really only be evaluated properly by review of survey and on-site inspection.

G. Evaluation of Sub-Surface Rights and Air Rights, if Appropriate.

1. Are there oil and gas leases burdening property?

2. Are air rights required and are they available?

H. Leases.

1. Understanding the rights of the tenant under all existing leases is of critical importance in evaluating the property. Do tenants have the right to terminate under any circumstances? Are there rights of first refusal to purchase property?

2. Understanding the tenants' obligations is also critical. Are tenants responsible for triple net rent ("NNN") reimbursements? Are tenants obligated for full reimbursement of NNNs or just increases from a base? What is base year and how does that bear on increases in property taxes, resulting from the sale itself (i.e. "uncapping")?

V. SELLER DELIVERABLES

Purchaser should require as many of the following as are in seller's possession or control:

A. Survey and Deeds.

B. Environmental Investigation Reports.

C. Tax Bills.

D. Certified Rent Roll.

E. Property Operating Statements.

F. Existing Warranties (e.g., roof, HVAC).

G. Leases and License Agreements.

H. Access Agreements.

I. Vendor Contracts Affecting Property.

J. List of Personal Property (multi-family).

K. Evidence of Governmental Violations.

VI. REPRESENTATIONS AND WARRANTIES

A. Seller will seek to limit warranties as much as possible and force purchaser to rely solely on purchaser's due diligence.

B. Purchaser typically seeks expansive representations. Compromise typically limits representations and warranties to seller's actual knowledge.

C. Relative bargaining power between the parties typically dictates the nature and extent of the seller's warranties and representations.

VII. TYPE OF DEED

A. When is a General Warranty Deed appropriate? These are almost always used in residential transactions. National and Michigan trend is away from General Warranty Deeds in commercial real estate transactions. Covenant Deed is the typical substitute.

B. Limited or Special Warranty Deeds, which are more and more common in other states, are not permitted in Michigan by statute.

C. Covenant Deed is used in Michigan instead of Limited or Special Warranty Deed.

D. General Warranty Deed warrants that the seller has good marketable title.

E. A Covenant Deed is the seller's agreement that it has not done anything to encumber title but does not warrant that seller received and holds good marketable title.

F. When is a Quit Claim Deed appropriate? Almost never in commercial real estate transactions. A Quit Claim deed only conveys whatever title the seller holds. Seller should be willing to at least offer a covenant to the purchaser that it has not created encumbrances on the property that would make the property unmarketable or will not be removed at or prior to closing.

G. When is a Fiduciary Deed appropriate? A Fiduciary Deed is similar to a Covenant Deed but is given by a fiduciary such as a Personal Representative of a decedent's estate or Trustee of a Trust.

VIII. ASSIGNMENT OF EXISTING LEASES AND OTHER RIGHTS

A. Assign the landlord's interest in the leases to the purchaser at closing.

B. Require seller to sign at closing notices to tenants regarding change of landlord, to assure smooth transition of rent payments.

C. Assign construction and other manufacturers' warranties.

D. Assign seller's rights to building plans, vendor contracts that are being assumed and the like.

E. Use Bill of Sale to convey seller's interest in personal property. Typically, only warranty in Bill of Sale relates to title and not condition of any property.

IX. OTHER KEY PROVISIONS

A. Estoppel Certificates/Subordination Non-Disturbance and Attornment Agreements.

If purchaser is obtaining financing for the purchase, it should be sure that Purchase Agreement requires that seller provide an Estoppel Certificate and Subordination, Non-Disturbance and Attornment Agreements ("SNDA") from each tenant, as its

lender will typically require them. Seller will seek to limit this requirement to only large tenants or only to some percentage of tenants. Negotiating this term often requires purchaser's consultation with its lender.

B. As Is / Where Is.

1. An "as-is" clause is a must for a Seller in a commercial real estate transaction (applies to residential as well). Purchasers of commercial property are expected to perform an extensive due diligence review and should not expect the seller to be responsible for adverse property conditions post-closing.

2. Purchaser will attempt to minimize its risk by extracting extensive warranties and representations. Seller will do the opposite and limit its post-closing liability as much as possible.

C. Closing Costs Allocation - Who Pays What?

1. Purchaser Typically Pays For:

   a. Pro-rations of current year property taxes paid in advance.

   b. Pro-rations of rents paid in advance.

   c. Recording fees for vesting deed.

   d. ½ of title company escrow fee.

   e. Purchaser's attorney fee.

   f. Purchaser's due diligence reports.

   g. Special Title Endorsements, including those requested by purchaser's lender.

2. Seller Typically Pays For:

   a. Base insurance premium.

   b. Transfer Tax (County: $.55 per $500 of sale price; State: $3.75 per $500 of sale price).

   c. Recording fees for instruments required to establish marketable title.

   d. ½ of title company escrow fee.

   e. Seller's attorney fee.

   f. In commercial transactions, the parties can agree to alternative allocation; although it is not commonly done.

D. Default Provisions.

1. Typical purchaser's default provision allows seller to retain earnest money deposit as sole remedy. It is virtually impossible to force purchaser to buy property with specific performance provision.

2. Typical seller's default provision allows purchaser to seek specific enforcement of purchase agreement (force seller to sell) or termination of purchase agreement with return of earnest money deposit. Purchaser may also seek recovery of out-of-pocket expenditures and other damages.

E. Notice, Time, Date Method.

Notice clause should provide for specific methodology for notification to other party; include email addresses and notification methodology. Be sure to specify when the notice becomes effective (e.g., at receipt of mailing or date of receipt). Failure to supply a notice procedure can lead to disputes when, for example, there is a dispute over whether a notice of termination was timely provided.

F. Risk of Loss.

Seller should be responsible for the risk of loss to the property until closing and should maintain insurance on the property until then.

G. Arbitration.

If Arbitration is desired, it should be specifically set forth in the agreement. If it is not, it will only be available if the parties mutually agree to do so. Arbitration can be an effective way of resolving disputes but has become a matter of personal preference, often based upon prior experience.

H. 1031 Exchange.

Both purchaser and seller may have the need or desire to engage in a tax deferred like-kind exchange permitted by Internal Revenue Code Section 1031. This may require some minimal cooperation from the other party so that the exacting requirements for a 1031 exchange are satisfied. Each party should agree to cooperate with the other party's 1031 exchange and even agree to sign confirming documentation so long as the same does not create liability or cost for the signer.

I. Survival.

Warranties, representations and covenants do not survive the closing unless specified otherwise; typically purchaser wants representations and warranties to survive closing indefinitely. Seller will seek to limit time frame for survival.

J. Post-Closing Occupancy.

Post-closing occupancy for the seller is much less common in commercial real estate transactions than residential transactions. However, if the purchaser agrees to allow the seller to remain in the premises after closing, a detailed post-closing occupancy agreement, akin to basic lease terms, should be created. At closing, most of the risks shift to the purchaser who will need significant protections for seller's on-going occupancy.

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Choice of Entity Strategies as They Relate to the New Tax Law

Gary Schwarcz

CHOICE OF ENTITY STRATEGIES AS THEY RELATE TO THE 2017 TAX ACT

I. C CORPORATION TAX CHANGES

A. Effective for all tax years after December 31, 2017, all C corporation taxable income will be subject to a tax at a flat 21% rate. Unlike most of the other changes under the Tax Cut and Jobs Act of 2017, Pub. Law 115-97 (the "Act" or "Tax Act"), this change is permanent.

B. Additionally, the Tax Act repeals the alternative minimum tax applicable to corporations.

C. Under pre-Act law, corporations that receive dividends from other corporations are entitled to a deduction for dividends received. If the corporation owns at least 20% of the stock of another corporation, an 80% dividends received deduction is allowed. Otherwise, a 70% deduction is allowed.

D. Under the Act, the 80% dividends received deduction is reduced to 65%, and the 70% dividends received deduction is reduced to 50%.

II. QUALIFIED BUSINESS INCOME DEDUCTION

A. For taxable years beginning after December 31, 2017 and prior to January 1, 2026, taxpayers, other than corporations, may generally deduct 20% of the combined qualified business income ("QBI") of an S corporation, partnership, LLC or a sole proprietorship allocable to such shareholder, partner, member or sole proprietor.

1. A taxpayer receiving the full benefit of the deduction would see a reduction in the taxpayer's top marginal rate on QBI to 29.6%.

2. The deduction reduces taxable income rather than adjusted gross income and is available to taxpayers who take the standard deduction.

B. Qualified business income is determined for each qualified trade or business of the taxpayer. A qualified business is a business other than: (1) "a specified service trade or business", or (2) "the business of performing services as an employee".

1. Qualified business income for a taxable year means the net amount of qualified items of income, gain, deduction, and loss with respect to the taxpayer's qualified business.

2. Items are treated as qualified only to the extent they are effectively connected with the conduct of a trade or business in the United States.

3. Qualified business income does not include: (1) reasonable compensation paid to the taxpayer by any qualified trade or business of the taxpayer for services rendered with respect to the trade or business; (2) guaranteed payment for services rendered with respect to the trade or business; or (3) to the extent provided in Treasury Regulations, any payment described in Code Section 707(a) to a partner for services rendered with respect to the trade or business.

Proposed Treasury Regulation Section 1.199A-3(b)(2)(ii)(H) provides that QBI does not include reasonable compensation paid by an S corporation but does not extend this rule to partnerships. The rule for reasonable compensation is merely a clarification that, even if an S corporation fails to pay a reasonable wage to its shareholder-employees, the shareholder-employees are nonetheless prevented from including an amount equal to reasonable compensation in QBI.

4. QBI does not include any amount paid by an S corporation that is treated as reasonable compensation of the taxpayer. Additionally, it does not include any guaranteed payments made by a partnership to a partner for services rendered with respect to the trade or business or any amounts paid by the partnership to the partner acting other than in his or her capacity as a partner for services.

5. Certain types of investment related items are excluded from QBI such as capital gains or losses, dividends and interest income (unless the interest is properly allocable to the business).

C. In order to obtain the full benefit of the deduction, the owner's taxable income must be less than $157,500 or less than $315,000 in the case of a married taxpayer filing jointly (the "threshold amounts").

<u>Example</u>: Assume Sam is the sole owner of a qualified trade or business through a disregarded LLC. The business has no employees and no substantial fixed assets. The QBI from the business is $175,000 and Sam's wife's taxable income is $100,000 resulting in a combined taxable income of $275,000. Since their joint taxable income is below the threshold amount of $315,000, Sam's deduction will equal 20% times $175,000 of QBI, or $35,000.

1. If the taxpayer's taxable income is less than the threshold amounts, the taxpayer will get the full benefit of the 20% deduction whether a qualified trade or business or a specified service trade or business.

2. However, even if the taxpayer's taxable income is below the threshold amounts, the QBI deduction is still limited to 20% of the excess of taxable income over net capital gain.

3. If the taxpayer's taxable income is above the fully phased in threshold amounts, $415,000 ($315,000 + $100,000) if married filing jointly, or $207,500 ($157,500 + $50,000) for other taxpayers, the QBI deduction is fully subject to wage and capital limits as a qualified trade or business (see II.D. below), or there is no deduction available in the case of a specified service trade or business.

4. The phase out of the QBI deduction for a specified service trade or business is $315,000 to $415,000 for married taxpayers filing jointly and $157,500 to $207,500 for all other taxpayers.

D. For business other than a "specified service trade or business" for which the taxpayer's taxable income exceeds the fully phased in threshold amounts, the deductible amount for each qualified trade or business carried on by the S corporation, partnership, LLC or sole proprietorship is the <u>lesser of</u>: (1) 20% of the taxpayer's allocable share of QBI with respect to the qualified trade or business; or

(2) the greater of (a) the taxpayer's allocable share of 50% of the W-2 wages with respect to the qualified trade or business, or (b) the taxpayer's allocable share of the sum of 25% of the qualified trade or business's W-2 wages, plus 2.5% of the unadjusted basis immediately after acquisition of all "qualified property".

1. W-2 wages do not include items such as payments to an independent contractor or management fees.

2. For purposes of Code Section 199A, "qualified property" means tangible property of a character subject to depreciation that is held by and available for use in the qualified trade or business at the close of the taxable year, is used in the production of QBI at some time during the taxable year, and has a depreciable period that has not expired before the close of the taxable year.

E. What is a qualified trade or business?

1. A qualified trade or business means any trade or business other than a "specified service trade or business" and other than the trade or business of being an employee.

2. Code Section 199A does not define trade or business for the purpose of the deduction.

   a. The Proposed Regulations state a "Trade or business" means a Code Section 162 trade or business other than the trade or business of performing services as an employee.

   b. There are a number of different interpretations of what may constitute a trade or business under the Code. In order for a trade or activity to be a trade or business under Code Section 162, the business must be regular, continuous and substantial.

   c. Would a triple net lease qualify as a trade or business for purposes of the Code Section 199A QBI deduction?

      Example: John's qualified trade or business generates $450,000 of QBI. His taxable income is also $450,000. If his trade or business is in the form of a sole proprietorship, John cannot pay himself a salary. Because John's taxable income is over the threshold amount as fully phased in, the W-2 limitation will apply and John's deduction will be zero.

      If John's qualified trade or business is in the form of a partnership, even if John pays himself a guaranteed payment of $175,000, the guaranteed payment will not qualify as W-2 wages and John's deduction will again be zero.

      If John operates as an S corporation, and pays himself a reasonable compensation amount of $150,000, John's deduction will equal the lesser of: (a) 20% of $300,000 of QBI ($450,000 QBI - $150,000

salary), or $60,000, or (b) 50% of $150,000 of W-2 wages, or $75,000.

Assume that John's business generates $250,000 of QBI and this is also his taxable income, his income is below the threshold amount.

If John operates as a sole proprietorship, he will be entitled to a deduction of 20% of $250,000, or $50,000.

If John's qualified business is in a partnership, since there are not guaranteed payments made by the partnership to John, John will again be entitled to a deduction equal to 20% of $250,000, or $50,000.

If, however, John's business is an S corporation, if John pays himself $100,000 of reasonable compensation, John's QBI will be reduced from $250,000 to $150,000 so that his deduction would only be $30,000 (20% of $150,000).

F. If there is more than one owner of a pass-through entity, the taxpayer is only entitled to the taxpayer's allocable share of QBI, W-2 wages and unadjusted basis of qualified property.

1. For an S corporation, the allocable share is relatively simple. It will equal the taxpayer's percentage ownership of the stock in the S corporation.

2. However, for partnerships where special allocations may be made under Code Section 704(b), a partner's allocable share of QBI and W-2 wages will be equal to the amount of ordinary income of the qualified trade or business allocated to the taxpayer by the partnership.

   Example: Frank is a 20% owner of an LLC which has QBI of $2,000,000. The LLC pays wages of $1,000,000 and the LLC's unadjusted basis in qualified property is $200,000. Frank's deduction will be equal to the lesser of: (1) Frank's allocable share of QBI ($2,000,000 x 20%, or $400,000) x the 20% deduction, or $80,000, and the greater of: (2)(a) Frank's allocable share of total wages ($1,000,000 x 20%, or $200,000) x the 50% W-2 limitation, or $100,000, or (2)(b) Frank's allocable share of total W-2 wages ($1,000,000 x 20%, or $200,000) x 25%, or $50,000, plus Frank's allocable share of unadjusted basis ($200,000 x 20%, or $40,000) x the 2.5% limitation, or $1,000, or in total $51,000. Thus, Frank is entitled to a deduction of $80,000.

3. The Proposed Treasury Regulations provide that:

   a. The Code Section 199A deduction, which is applied at the partner or shareholder level in the case of a partnership or S corporation under Code Section 199A(f)(1), has no effect on either the adjusted basis of the partner's interest in the partnership or the shareholder's stock in an S corporation, or the S corporation's accumulated adjustments account.

b. The Code Section 199A deduction does not reduce net earnings from self-employment under Code Section 1402 or net investment income under Code Section 1411.

G. In the Proposed Treasury Regulations, the IRS provided that if certain requirements are met, individuals who engage in more than one trade or business may—but are not required to—aggregate trades and businesses, treating them as a single trade or business for purposes of applying the limitations described in Proposed Regulation Section 1.199A-1(d)(2)(iv) (i.e., the QBI component calculation).

1. In general, trades or businesses may be aggregated only if an individual can demonstrate that the following "aggregation requirements" are satisfied:

    a. The same person or group of persons, directly or indirectly, owns 50% or more of each trade or business to be aggregated, meaning in the case of such trades or businesses owned by an S corporation, 50% or more of the issued and outstanding shares of the corporation, or, in the case of such trades or businesses owned by a partnership, 50% or more of the capital or profits in the partnership (50% ownership requirement);

    b. The 50% ownership requirement is met for a majority of the tax year in which the items attributable to each trade or business to be aggregated are included in income;

    c. All of the items attributable to each trade or business to be aggregated are reported on returns with the same tax year, not taking into account short tax years;

    d. None of the trades or businesses to be aggregated is a specified service trade or business ("SSTB") as defined in Proposed Regulation Section 1.199A-5; and

2. The trades or businesses to be aggregated must satisfy at least two of the following three factors, based on all of the facts and circumstances, which demonstrate that the businesses are in fact part of a larger, integrated trade or business: (1) they provide products and services that are the same or customarily offered together (e.g., a gas station and a car wash); (2) they share facilities or share significant centralized business elements, such as personnel, accounting, legal, manufacturing, purchasing, human resources, or information technology resources; and/or (3) they are operated in coordination with, or reliance upon, one or more of the businesses in the aggregated group.

3. An individual may aggregate trades or businesses operated directly and the individual's share of QBI, W-2 wages, and unadjusted basis immediately after acquisition ("UBIA") of qualified property from trades or businesses operated through relevant pass-through entities ("RPEs"). Multiple owners of an RPE need not aggregate in the same manner.

4. An individual directly engaged in a trade or business must compute QBI, W-2 wages, and UBIA of qualified property for each trade or business before applying the aggregation rules. If an individual aggregates multiple trades or businesses,

the individual must combine the QBI, W-2 wages, and UBIA of qualified property for all aggregated trades or businesses for purposes of applying the W-2 wage and UBIA of qualified property limitations described in Proposed Regulation Section 1.199A-1(d)(2)(iv).

5. For purposes of determining ownership for purposes of the 50% ownership requirement, an individual is considered as owning the interest in each trade or business owned, directly or indirectly, by or for:

   a. The individual's spouse (other than a spouse who is legally separated from the individual under a decree of divorce or separate maintenance); and

   b. The individual's children, grandchildren, and parents.

H. Code Section 199A defines a specified service trade or business as any trade or business which involves the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services where the principal asset of the trade or business is the reputation or skill of one or more of its employees or owners or which involves the performance of services that consist of investing and investment management, trading or dealing in securities, partnership interests or commodities.

   1. Although a specified service trade or business is not a qualified trade or business, a taxpayer in such a business may still be eligible for the 20% QBI deduction provided that the taxpayer's taxable income is less than the threshold amounts.

      Example: Lisa is a partner in an accounting firm operated as a partnership. Lisa has total taxable income with her husband of $250,000. Lisa's allocable share of the accounting firm's QBI is $200,000, her share of W-2 wages of the accounting firm is $50,000 and her share of the unadjusted basis of the qualified property of the accounting firm is $30,000. Although Lisa derives her income from a specified service trade or business, she will still receive a deduction of $40,000 ($200,000 x 20%), because Lisa's income is below the threshold amount. The W-2 limitation and/or the adjusted basis limitation will not be applicable because her taxable income is below the threshold amount.

   2. The QBI deduction will not be available at all for shareholders, partners, members or sole proprietors of a specified service trade or business whose taxable income exceeds the fully phased out threshold amounts.

      Example: Jennifer is a partner in a medical practice. Jennifer is married and has taxable income of $750,000. Jennifer's allocable share of income from the medical practice is $500,000, her allocable share of W-2 wages from the medical practice is $150,000 and her share of the unadjusted basis of qualified property is $100,000. Jennifer is not entitled to a deduction at all because the medical practice is a specified service trade or business and her income exceeds the married filing jointly phase out threshold amount of $415,000.

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I. Notwithstanding all of the previously mentioned limitations, the deduction under Code Section 199A cannot exceed 20% of the excess of the taxpayer's taxable income less any capital gain for the taxable year.

   Example: Rachel is married and has $100,000 of QBI. She has $100,000 of long term capital gain, $30,000 of wages and $50,000 of itemized deductions resulting in taxable income of $180,000. Rachel's deduction will be limited to the lesser of: (1) 20% of QBI of $100,000, or $20,000, or (2) 20% of $180,000 of taxable income less $100,000 of capital gain, or $16,000.

J. If the taxpayer's net amount of qualified business income from all qualified trades or businesses is a loss, it is carried forward and treated as a loss from a qualified trade or business in the next tax year.

III. CHOICE OF ENTITY

A. Because of the rules previously stated, there can be significantly different tax results between S corporations, partnerships and sole proprietorships having the same amount of income. This may affect the taxpayer's choice of entity decisions.

   As a result of the reduced corporate tax rate applicable to C corporations of 21%, and the 20% QBI deduction for pass-through entities, the choice of entity may be affected, especially where the entity is not planning on distributing available cash to its owners.

B. While businesses used to default to organizing as pass through entities to avoid a high corporate tax rate and double taxation, the drop in the corporate tax rate from 35 percent to 21 percent may require planners to engage in a careful cost-benefit analysis to determine which structure is the most beneficial.

C. As a result of the reduced corporate tax rate applicable to C corporations of 21%, and the 20% QBI deduction for pass-through entities, the choice of entity may be affected, especially where the entity is not planning on distributing available cash to its owners.

D. Note that if an S corporation is chosen as the choice of entity, the shareholder may not receive unreasonably low compensation. The IRS may challenge reported wages in re-characterizing S corporation distributions as wages where the IRS determines that unreasonably low compensation has been paid to the shareholder-employee. This reclassification does not appear to apply to partnerships and sole proprietorships under current law.

E. Unlike S corporations which pay W-2 wages to their shareholder-employees, W-2 wages cannot be paid to a partner of a partnership or to a sole proprietor resulting in the wage limitation being equal to zero where the qualified trade or business has no outside employees.

F. Where a qualifying trade or business does not have depreciable property or any wages other than those paid to the owner of the business, a determination should be made on the amount of W-2 compensation to be paid to the owner so that the W-2

limit is not zero, while the same time leaving some QBI on which to apply the 20% since any reasonable compensation will reduce the QBI.

G. While C corporations will continue to be subject to the "double tax" on their earnings, once at the corporate level and again at the shareholder level, when the earnings of the corporation are distributed to its shareholders, the maximum combined double tax rate will be reduced to 36.8% (or 39.8% if the Net Investment Income Tax is applicable). Additionally, some states still impose a corporate income tax on C corporations but not on S corporations, partnerships, LLCs or sole proprietorships.

H. The top marginal tax rate on the income of a pass-through entity or a sole proprietorship is 37% even if the taxpayer does not receive any Code Section 199A deduction. If the Code Section 199A deduction is applicable, the marginal tax rate is 29.6% on the QBI of a pass-through entity or sole proprietorship.

I. To the extent a C corporation is not distributing its earnings, however, and the 21% corporate tax rate is applicable, consideration must be given to (1) the necessity for reasonable compensation, (2) the accumulated earnings tax, and (3) the personal holding company tax.

J. Consideration must be given to whether a future Congress will retain the 21% C corporation tax rate.

K. In the event a C corporation sells its assets and distributes the proceeds to its shareholders, the combined double tax rate will be 36.8%, or 39.8% if the 3.8% Net Investment Income Tax is applicable. If a pass-through entity or sole proprietorship sells its assets, where most of the assets are capital assets (such as goodwill), the maximum marginal tax rate on the capital gain resulting from the sale of assets will either be 20%, or 23.8% if the Net Investment Income Tax is applicable.

L. If Congress raises the C corporation tax rates, shareholders may find themselves stuck in C corporation status.

    1. If a C corporation converts to a partnership or sole proprietorship, the conversion will be taxed as a liquidation.

    2. Where an S corporation has revoked its S election status to become a C corporation, the Corporation will generally be prohibited from a re-electing S status for a period of 5 years.

    3. Even if a C corporation is allowed to convert to S corporation status, there remain a number of unfavorable rules that may apply to the S corporation such as the application of the LIFO recapture tax, the imposition of tax on excessive passive investment income or for S corporations having subchapter C earnings and profits, the possible termination of the corporation's S election where it has excess passive investment income and subchapter C earnings and profits for three (3) consecutive years, and the less favorable distribution rules applicable to S corporations having C corporation earnings and profits vs. S corporations having no C corporation earnings and profits.

4. Finally, the built-in gains tax is imposed on C corporations which have converted to S corporations, resulting in double tax to the extent of any built-in gain, if the assets of the corporation are sold or otherwise disposed of within the five (5) year period following the corporation's conversion to S status.

M. Notwithstanding the Tax Act changes, one must still consider whether the Subchapter S rules versus the Subchapter K rules are more favorable for a particular client (for example with rental real estate).

Avoiding Discrimination and Harassment in the Workplace - A Guide for Small Employers

David A. Lawrence

AVOIDING DISCRIMINATION AND HARASSMENT IN THE WORKPLACE
A GUIDE FOR SMALL EMPLOYERS

I. DEFINING DISCRIMINATION AND HARASSMENT

A. What is Discrimination?

1. In general, it is illegal to discriminate in employment opportunities, decisions or practices on the basis of race, color, religion, sex, national origin, age, weight, height, disability, familial, marital or veteran status or any other characteristic protected by law. Some of the relevant federal and state laws are:

   a. Title VII of the Civil Rights Act of 1964 (federal), 42 USC 2000d et seq., prohibits employers from discriminating against employees on the basis of sex, race, color, national origin and religion. Generally applies to employers with 15 or more employees.

   b. The Elliot-Larsen Civil Rights Act, MCL 37.2101 et seq., is Michigan's version of Title VII, but broader. It prohibits discrimination on the basis of race, color, religion, national origin, age, sex (including pregnancy), height, weight, or marital status. Elliott-Larsen covers all employers.

   c. The Americans with Disabilities Act of 1990 (federal), 42 USC 12101 et seq., prohibits discrimination against individuals with disabilities who are qualified to perform the essential functions of the job, with or without reasonable accommodation. This applies to all stages of employment and requires the employer to make reasonable accommodations for employees with disabilities. Generally applies to employers with 15 or more employees.

   d. Michigan's Persons with Disabilities Civil Rights Act, MCL 37.1101 et seq., also prohibits discrimination against an individual with a disability who is otherwise qualified to perform the essential functions of the job. Like the ADA, it applies to all stages of employment and requires the employer to make reasonable accommodations for employees with disabilities.

   e. The Equal Pay Act of 1963, as amended (federal), Pub L. 88-38, 29 USC 206(d) et seq., prohibits sex-based wage discrimination between men and women in the same establishment who perform jobs that require substantially equal skill, effort and responsibility under similar working conditions. Virtually all employers are covered.

   f. The Age Discrimination in Employment Act (federal), 29 USC 621 et seq., prohibits employment discrimination against anyone 40 years of age or older, but does not protect certain types of employees, such as bona fide executives and high policymakers. Generally applies to employers with 20 or more employees.

2. Discrimination based upon sexual orientation.

   a. There is no federal law that expressly outlaws workplace discrimination on the basis of sexual orientation by private employers. However, the Equal Employment Opportunity Commission ('EEOC") has recently taken the position that sexual orientation discrimination is generally illegal under Title VII (as sex-based discrimination). Some federal appeals courts, including the Sixth Circuit Court of Appeals which covers Michigan, have agreed in several situations.

   b. Similarly, nothing in Michigan's law expressly prohibits discrimination on the basis of sexual orientation. However, in May 2018 the Michigan Civil Rights Commission issued a statement that the word "sex" in Elliot-Larsen includes sexual orientation and gender identity. Attorney General Bill Schuette then issued an opinion saying the Commission was wrong and had overstepped its authority. However, the Commission has ignored Schuette's opinion and has directed the Michigan Department of Civil Rights ("MDCR") to continue investigating such complaints.

   c. For now the law is somewhat unsettled but employers in Michigan should err on the side of caution.

B. Favoritism is NOT Discrimination. Some types of unequal treatment are perfectly legal. An employer or manager may show favoritism toward certain employees based upon factors that are not protected. For example, they may favor a family member, an employee that graduated from the same college as they did, or the employee with whom they socialize after work. Favortism may be bad management, but it is usually not illegal.

C. What is Illegal Harassment?

   1. <u>Harassment is not limited to sexual harassment</u>. Illegal harassment is any unwelcome or unsolicited verbal or physical conduct that denigrates or shows hostility or aversion toward an individual due to his or her race, color, religion, gender, national origin, age, or disability. Employers should be vigilant to prevent any kind of harassment.

   2. The EEOC defines <u>sexual harassment</u> as unwelcome verbal or physical conduct of a sexual nature when: (i) submission to such conduct is made a term or condition of employment; (ii) submission to or rejection of such conduct is used as a basis for employment decisions; or (iii) such conduct unreasonably interferes with job performance or creates an intimidating, hostile, or offensive work environment.

D. Retaliation is also illegal. An employer (and its managers) may not retaliate against an applicant or employee for filing or being a witness in any discrimination or

harassment charge, complaint, investigation or lawsuit, or for engaging in other acts to oppose discrimination or harassment in the workplace.

E. Lawsuits & Complaints.

1. Most discrimination claims are first filed with the EEOC (federal) or MDCR (state). The agency will conduct mediation and/or investigate the claim and issue a Dismissal and Notice of Rights. If the Charge is not resolved by the EEOC, the employee may file suit in court within 90 days.

2. The EEOC reports that employment discrimination claims are on the rise and have been for several years. A total of 84,254 charges were filed with the EEOC during fiscal year 2017.

3. Retaliation is the most frequently cited bases for complaints (49%). The next most common complaints are related to race (34%), disability (32%) and sex (30.5%). Many charges allege multiple bases.

4. Regardless of whether an employee's complaint has merit, the employer is going to have to invest time, effort and money to address it. In addition to the legal costs, the employer may suffer from loss of employee morale, reduced productivity, and loss of reputation.

II. WORKPLACE SITUATIONS WHERE DISCRIMINATION AND HARASSMENT MAY OCCUR

A. Recruitment and Hiring.

1. Job Postings and Prescreening Tests: Any stated criteria or required testing should be directly related to the position.

2. Interviews: Do not ask applicant their age, religion or nationality.

3. Employers cannot ask an applicant if they have a disability, but can ask if they are able to perform essential functions of the job with or without a reasonable accommodation.

4. Be consistent. Hiring procedures should be consistent for every applicant.

B. Terminations and Restructuring.

1. Dismissing an employee for a legitimate reason (e.g. poor work performance or business restructuring) could still result in a claim for "wrongful termination" if an employee believes the cited reason is a pretext for unlawful discrimination.

2. Any employee disciplinary or performance issues should be documented.

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C. Compensation, Promotion and Training Opportunities.

1. Compensation discrimination occurs when employees performing substantially the same work in the same circumstances do not receive the same rate of pay. Employees performing jobs that require substantially the same skill, effort, responsibility, and under similar working conditions must be compensated equally for their time. Differences in pay are permitted based upon seniority, merit and quantity or quality of performance.

2. Employers often make promotion and training decisions based upon subjective factors. This may lead employees to complain that they were unfairly passed over. Employers should be specific about the requirements for promotion and training opportunities. Promotions should be based upon a fair and consistent process and neutral criteria that don't create barriers to protected categories of workers.

D. Co-workers and Supervisors.

1. Employers may be liable for discrimination or harassment committed by supervisors or co-workers or others.

2. Supervisors: When harassment by a supervisor results in adverse employment action against an employee, the employer is automatically liable. If no tangible action against the employee occurred, the employer may assert an affirmative defense if it exercised reasonable care to prevent and correct promptly any harassing behaviors.

3. Co-Workers and Non-Employees: Employers are liable for the harassment of co-workers and non-employees only if the employer knew or should have known and failed to take prompt remedial action. A "hostile work environment" arises from comments or conduct that have the purpose or effect of unreasonably interfering with an individual's work performance or creating an intimidating or offensive working environment. Anyone can create a hostile work environment - a co-worker, supervisor or even a non-employee. As a result, an employer is also liable if it knew or should have known about the harassment and failed to take immediate and appropriate corrective action.

4. Employers should promptly investigate any reports of harassment or discrimination between co-workers or by supervisors. Early intervention and resolution may prevent a formal claim.

III. AVOIDING DISCRIMINATION AND HARASSMENT

A. Written Policies.

1. Employers should have a written policy prohibiting discrimination and harassment. The policy should clearly state that discrimination and harassment

will not be tolerated and that employees engaging in such behavior may be disciplined.

2. As part of the policy there should be a clear procedure instructing employees how to report claims of discrimination and harassment, and explaining how the employer will investigate such claims.

3. The policy should emphasize that there will be no retaliation against employees who file claims.

B. Training.

1. Managers should be trained to properly follow anti-discrimination laws and implement the employer's written policies with the expectation that prevention is their responsibility.

2. Employees should be trained to properly recognize and prevent workplace harassment with the expectation that maintaining a work environment that discourages discrimination, harassment and retaliation is part of their job responsibilities.

C. Documentation. Employers should document all aspects of policy training, complaint investigation, hiring and promotion practices, management development and employee preventative training.

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