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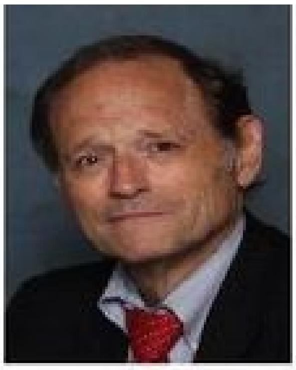

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Re: Reduce Risk by Segregating Assets in a New Entity

(And Not Triggering An Income Tax!)

The Problem: Often business owners want to segregate valuable assets from potential adverse liabilities generated in the operation of a business. For example, a bakery will likely own: (1) equipment used in its operations; (2) the factory building and (3) a fleet of delivery trucks and vehicles. If all of these are owned by the same company, then liabilities arising from an accident involving the trucks could result in the loss of the factory building to satisfy a judgment. This is true for any asset held by the company, especially if the company has been in business for many years and has accumulated other assets not directly involved in the baking operation. A better arrangement would be for the trucks to be in a new company and then lease them to the bakery, which is in the old corporation.

If property is transferred from the company, then the company would be treated as having sold the property triggering an income tax at the corporate level, and then the shareholders would pay another tax at their level, probably taxed as dividends.

A Solution: Assume that a new entity was formed to be the holding company parent, that is, holding all the stock of the old company, and then a second new company was formed, whose stock was also held by the new holding company parent, then the trucks could be held in the new subsidiary company while all the other old assets were retained in the old subsidiary company.

The IRS has ruled in a private letter ruling that this arrangement was “F” reorganization and there would be no income tax to any of the parties to the reorganization. The IRS’s opinion stated that since the ownership has not changed, the business has not changed and the assets have not changed either, then nothing really happened, so the transaction is a tax-free reorganization.

This is a viable way to do some asset protection reorganizing at no tax cost. There is some estate planning that can be done here as well. Some assets needing protection might be placed in an entity for different purposes, such as factoring of accounts receivable, buildings, equipment, marketable securities, etc., and more.