

VIEW FROM THE TOP

TREETOP VENTURES NEWSLETTER

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It Works ...

By William Fisher



One of the more exciting things that happened in our world this year was the announcement back in the first part of the year regarding Angel Tax Credits for investors in start-ups. For those of us who are involved in funding start-up's, this was something that we felt was sorely needed. We had heard about other programs in other states (Kansas being one that had a great program) but I think we were surprised with the speed in which this passed through the legislative side of the house. We first read about it in late spring and it was announced as a 'go' in late August.

For one of our investments, the timing couldn't have been better. We were in the process of raising a round of capital for Financial Transmission Network, Inc., the local payment hub that was founded by Kurt Matis. We hustled to get our hands on the early information regarding who qualified and, after reading through the literature, decided the company was a fit. Now, all we had to do was complete the paperwork.

Yikes!

Actually, it wasn't that bad but it was definitely an iterative process. Kurt and his staff had a lot of work to do on this and unfortunately, even though Kurt was an investor on all previous rounds and also on this round, he wasn't eligible for the tax credit. We would like to see this change; investors like founders to have their skin in the game but for various reasons the legislature excluded anyone who owned more than a certain percentage or obtained more than a certain percent of their income from the business. I assume they are trying to eliminate self-dealing; however, we feel it can be done in a different manner and would truly help the program if founders were allowed to get the benefit of the credit.

Even though Kurt and his senior staff who invested were not eligible, they understood the value for their investors and worked hard to get the necessary information to the state on a timely basis.

First, you must qualify the company as a company headquartered in Nebraska, engaged in a specific discipline that fits the state criteria and with a payroll that is more than 50% within the state of Nebraska. You must go to the government web site (e-verify) and make sure that your employees are citizens plus provide copies of the payroll register to the state. You must also provide a Certificate of Good Standing for the business from the state (this wasn't listed a requirement; part of the iterative process that was somewhat frustrating).

Next, the investors must be certified as 'pass through entities' who can utilize the tax credit within Nebraska. They must be Nebraska tax payers (another issue; what is wrong with money coming in from outside the state) primarily due to the complication of providing credits to someone who isn't a Nebraska taxpayer. (FYI: Kansas doesn't have this restriction). The investors must also attach a form that attests that they are citizens.

Once they are certified, the next step is to apply for tax credits based on a form that outlines the amount and timing of the investment. Almost there; however, need the state to tell us that there are tax credits to be had and that we qualify if we make the investment.

Now, we make the investment and then the company provides detailed information that shows that an investment was made by the individual. This includes a copy of the signed shareholder agreement, a copy of the check to the firm and a copy of the deposit

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Tax Incentives for New Businesses in 2011 and Beyond: Deducting Organizational and Startup Costs

(Corporation, LLC or Partnership)

By Pam Knutson

As you start your new business, keep the money in your business instead of giving it to the government by taking advantage of the tax incentives available to you. Keep in mind what you can deduct immediately and what you have to amortize, or expense, over a period of time.

In the year you start your business, you can expense up to \$5,000 of your startup costs and \$5,000 of your organizational costs. Additional costs over each \$5,000 limit can be amortized over 15 years, with costs over \$50,000 having additional restrictions. First let's define startup costs and organizational costs.

What's the difference between the two? Startup costs are incurred before the day your active trade or business begins.

Investigatory Startup Costs

The first category of startup costs is investigatory. These costs relate to your decision whether to start or purchase a business and which particular business to start or purchase. Examples:

- analysis of products, labor supply, and transportation facilities
- fees for consultants and professional services
- surveys of potential markets
- travel costs for securing distributors, suppliers, and customers

Preopening Startup Costs

The second category of startup costs is preopening costs. These are costs incurred after you have made a decision to take the plunge, but before your business actually begins. Examples:

- Advertising the opening of the business
- Promotional items for the grand opening
- Salaries to employees for training (and their instructors)
- Salaries to executives
- Repairs
- Utilities

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It Works ... (continued)

slip showing that the copy deposited the check.

Once the state has this data, they have up to 30 days to send the investors letters telling them that they have a tax credit and the amount. In the case of FTNI, it was a 40% tax credit so an investor that invested \$100,000 in the round got a \$40,000 tax credit from the State of Nebraska. When they file taxes for 2011 in 2012, the state tax form will have a box to check for a tax credit and these monies will be applied at that time. For most of you that do proper tax planning and don't anticipate owing the state any extra monies, this credit will flow back to you in the form of a refund check.

We started on this process the last week in August and received final vouchers outlining tax credits the week of Thanksgiving. We had a few hiccups, had to get investors to sign some documents but all in all, everyone was happy to get a 40% tax credit for making an investment in a local company.

Going forward, we expect to help companies navigate through the filing and approval process and are hopeful that we can effectively lobby for changes so that our founders can also benefit from this. If we can help you, let us know.

Recordkeeping Relief Provided by IRS to Small Businesses

No, Hell did NOT freeze over!

By Pam Knutson

On September 14, 2011, the IRS issued a Notice providing guidance on a provision in the Small Business Jobs Act of 2010 regarding the tax treatment of employer-provided cell phones. The 2010 Act removed cell phones from the definition of listed property, a category under tax law that normally requires additional recordkeeping by taxpayers.

The September 14 Notice states that when an employer provides an employee with a cell phone primarily for noncompensatory business reasons, the business AND personal use of the cell phone is generally nontaxable to the employee. In addition, the IRS will NOT require recordkeeping of business use in order to consider the cell phone an excludible fringe benefit.

The IRS also announced in a memo to its examiners that a similar approach will be taken where employers provide their employees cash allowances or reimbursements for business use of their personal cell phones. In this situation, payments to the employees for reasonable cell phone coverage are nontaxable.

It is wise to note that, in either scenario, if cell-phone use is not primarily business related, the arrangement is generally taxable.

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Tax Incentives for New Businesses in 2011 and Beyond ... (continued)

Startup costs do not include deductible interest, taxes or research and experimental costs. You can still deduct those items, but they are not startup costs that qualify for the special tax treatment.

Organizational Costs

Organizational costs begin as you create (organize) your business entity.

Examples of deductible costs associated with organizing a corporation:

- Accounting fees to set up the corporation's books
- Costs of organizational meetings
- Costs of temporary directors
- Legal fees to draft the corporate charter, bylaws, minutes of organizational meetings, and terms of original stock certificates
- State incorporation fees

Examples for organizing a partnership:

- Accounting fees to set up the partnership's books
- Filing fees
- Legal fees for negotiation and preparation of the partnership agreement

Costs that do not qualify as organizational costs for corporations are:

- Commissions
- Professional fees and printing costs for issuing and selling stock
- Costs incurred for transferring assets to the corporation

These costs are classified as capital expenses and are part of the basis of your business and are recovered only when you dispose of your business.

Partnerships cannot classify these as organizational costs:

- Cost of transferring assets to the partnership
- Cost of making a contract regarding the operation of the partnership
- Costs of preparing a prospectus
- Syndication costs of marketing and issuing partnership interests

Should I deduct or amortize?

Good question. If you are not going to be profitable in your first year, you may want to consider amortizing them over 15 years rather than decreasing your profitability further by increasing your expenses.

Your tax accountant can help you classify your expenses and advise you about deducting or amortizing for full advantage of the 2011 new business tax incentives. Just make sure you save receipts and invoices from vendors that fully describe the services.

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