Wage And Hour Issues

By Margherita M. Albarello

Dine-in and Other Movie Theaters Targeted by DOL for Child Labor Violations

Don’t be surprised if you hear a public service announcement on workplace safety the next time you go to the cinema. In March, the U.S. Department of Labor assessed civil penalties of over $275,000 against three movie theater companies with operations in Illinois, Wisconsin, and seven other states for allowing minors to perform hazardous jobs like operating trash compactors, using power-driven dough mixers, and baking. The movie theater industry has a high rate of non-compliance with child labor laws. With the advent of dine-in movie theaters, increasing numbers of minors are being asked to operate power-driven bakery machines and to do baking work.

The operation of power-driven bakery machines is one of 17 “particularly hazardous” non-farm jobs which the U.S. Secretary of Labor says is a no-no for teens below the age of 18. The Secretary also prohibits 14 and 15-year old employees from baking or cooking, with the exception of cooking with electric or gas grills which do not involve working over an open flame or cooking with deep fryers equipped with a device which automatically lowers and raises the baskets into and from the hot oil. In addition to paying financial penalties, the affected companies agreed to implement comprehensive internal compliance and training programs for managers and to make public service announcements about child labor safety on the big screen.

In our last issue, we examined the changes to the federal estate tax law passed by Congress in December of 2010, which raised the threshold for federal estate tax to its highest amount ever, $5 Million. This law has a significant impact on our estate planning, as the $5 Million amount gives up to $10 Million of “coverage” for married clients, thereby allowing most of our clients to avoid federal estate tax liability. But, as we set forth last issue, the amount is only guaranteed for two years.

Our planners, however, even now cannot completely rely on the $5 Million amount for resolving estate tax exposures, as Illinois has its own estate tax, which takes effect at taxable estate levels of only $2 Million. Thus, if an Illinois resident dies with an estate of, for example, $3 Million (including life insurance, deferred compensation and all other assets), while there would be no federal estate tax because the estate is below the $5 Million threshold, there would be an Illinois estate tax because the estate exceeds $2 Million. The Illinois estate tax rates begin at 8% and go as high as 16%, so in this example the Illinois estate tax would be in excess of $167,000.

The Illinois estate tax has not always been known as an estate tax. Rather, until January 1, 1983, it was known as the Illinois Inheritance Tax. The tax was levied upon the recipients of inherited property, rather than on the estate itself. Even for surviving spouses, the tax could apply for assets totaling beginning at only $20,000! It was a hugely unpopular tax, and had to be enforced by the Illinois Attorney General’s office. Thus, upon learning of the death of one of its depositors or safe deposit box holders, banks were obligated to “freeze” the decedent’s account until a release of the inheritance tax lien could be secured from the Attorney General’s office. Banks actually kept an employee on staff whose job it was to scan the obituary pages of the local newspapers to cross-reference the decedents against their customer list. Funeral directors and attorneys had to direct their surviving clients to rush to the bank to withdraw living expense money before the bank became aware of the death, as the banks had no choice but to freeze the accounts. Estate administration attorneys spent an inordinate amount of their time in those days securing releases for frozen assets.

The inheritance tax was finally abolished January 1st of 1983, to be replaced by the present estate tax system. The replacement Illinois estate tax was basically a “pick-up” tax, whereby there could be no Illinois estate tax unless there was a federal estate tax, and the amount of the Illinois tax was equal to a portion of the federal tax, shared by the federal government with the state. Many states have this system, which is obviously more survivor-friendly than the old inheritance tax system. And estate planning attorneys could do their tax planning solely with an eye toward dealing with the federal estate tax laws, as no additional, separate Illinois tax was possible.

This system worked seamlessly until the federal estate tax exempt amount began to rise steeply in the late 2000s. From 2001 through 2008, the amount grew gradually from $1 Million to $2 Million, but in 2009 jumped to $3.5 Million. When that happened, many states, including Illinois, “de-coupled” from the federal estate tax format and passed new estate tax laws providing that the state estate tax began at a lower amount than $3.5 Million. Thus, Illinois now has the $2 Million threshold for estate tax, and when the federal estate tax threshold amount was raised last December to $5 Million, Illinois again remained at $2 Million. Thus, the amounts between $2 Million and $5 Million are subject to Illinois tax only, and our estate planning counsel must now adjust our client’s existing estate planning documents to respond to that change.

Some amendments to existing trusts and wills are required to maximize our clients’ protection from the state estate tax, especially in the case of married taxpayers. With proper drafting, it is still possible to have no state or federal tax due on the death of the first spouse to die. A spouse with an estate of $5,000,000 or more, who uses the special QTIP election can defer up to $352,158 in Illinois estate taxes that would otherwise be payable upon the death of the first spouse.

We urge our clients whose total joint net worth approaches $2 Million to consult with our estate planning counsel to determine whether modifications to their estate plan could be helpful.
2011: The Year For Giving
By: Adam J. Poteracki

In December 2010, Congress passed the Tax Relief, Unemployment Insurance Re-authorization, and Job Creation Act of 2010, which, among other things, provided a temporary resolution to federal estate and gift tax uncertainty. Lee Poteracki discussed the general provisions of the 2010 Act in an article published in the January 2011 edition of this Newsletter. This article is intended to discuss opportunities for gift planning presented in the 2010 Act.

The 2010 Act re-unifies the Federal Estate and Gift Tax exclusion amount at $5 Million. As a result, an individual can make taxable gifts in 2011 or 2012 of up to $5 Million before incurring any gift tax.

Although the nominal rate of Estate Tax and Gift Tax are each 35%, making lifetime taxable gifts has the potential to avoid more taxes than waiting for property to pass at death. The following three considerations make planned lifetime gifting a valuable tool in constructing an estate plan that aims for tax avoidance.

First, the gift tax is a tax-exclusive tax, paid for out of money that is not being taxed. The estate tax is a tax-inclusive tax, paid for out of money that is being taxed. The following example illustrates the benefit of paying a tax-exclusive tax rather than a tax-inclusive tax:

A has $5 Million in assets and has already used the entire $5 Million exclusion on other lifetime gifts. If A chooses to not make any gifts, A’s estate will pay $1.75 Million in federal estate tax and $3.25 Million will be passed along to A’s beneficiary, B. However, if A chooses to make a lifetime gift of $3 Million to B, A will pay $1.05 Million in gift tax and the remaining $950,000.00 will be subject to estate tax at A’s death. A’s estate will pay $332,500.00 in federal estate taxes, leaving an additional $617,500.00 for B. By taking advantage of the gift tax, A will pass over $3.6 Million to B and only pay slightly more than $1.3 Million in combined federal estate and gift taxes.

Lifetime gifting allows A to pass more assets to B and pay less in taxes because A is taking advantage of the tax-exclusive nature of the gift tax.

Secondly, lifetime gifting allows you to apply the $5 Million exclusion to assets before the assets appreciate. Clearly, it would be preferable to use up part of the $5 Million exclusion on an asset worth $3 Million today rather than to use up the entire $5 Million exclusion and pay estate taxes on $1 Million on that same asset several years from now when it is worth $6 Million. Of course, it is important to first target assets that you expect to appreciate. You should be careful to plan your gifting, especially when attempting to take advantage of unappreciated assets.

A third benefit of gifting is that it enables the planner to make use of a certain exclusion. As we have previously advised, the 2010 Act is temporary. The current $5 Million exclusion is only in effect through the end of 2012. After 2012, there is no guaranty that a $5 Million exclusion will be available for federal estate and gift tax purposes. Gifting prior to 2012 ensures you will be able to take advantage of the $5 Million exclusion.

There are clear opportunities for tax avoidance by planned gifting from now through 2012. Non-tax considerations also must be taken into account. A planned gifting program should only be undertaken after careful consultation with our estate planning counsel.

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Child labor is work that harms children or keeps them from attending school. “Harm” comes in many forms, including losing an eye to a nail gun or being sexually exploited while working as a hotel maid. Federal and state child labor laws dictate what workers under 18 years of age can do and how many and what hours in a day or week they can work. Many employers will hire high school students for the summer. Now is the time to conduct a self-audit of what work you need performed and when and what age groups can legally perform the work to be done. This will help you in making appropriate hiring decisions.

Do you need workers to do tasks which are declared “hazardous” by the Secretary of Labor, like driving a car or truck, using power-driven wood-working, metal-forming, or bakery machines? If so, then don’t hire anyone under age 18.

Do you need workers to stand at busy intersections as “sign wavers” to hawk your latest promotion or store relocation? If so, then don’t hire anyone under age 16, as federal law prohibits this employment unless performed directly in front of your establishment.

Do you need workers to vacuum carpets and use floor waxes? If so, you are free to hire 14 and 15-year olds and their mothers will thank you.

Do you need workers to rent shoes at your bowling alley? If the bowling alley is in Illinois, then anyone under age 16 is off limits.

Will you be asking teens to work unlimited hours or hours beyond 9 p.m.? Teens 16 and 17 years old may perform any nonhazardous job for unlimited hours. Teens 14 and 15 years old may work outside of school hours in certain jobs up to three hours on a school day and 18 hours during a school week, and eight hours on a non-school day and 40 hours during a non-school week. Work must be performed between the hours of 7 a.m. and 7 p.m., except from June 1 through Labor Day, when evening hours are extended to 9 p.m.

No matter what job the teen is performing, stress safety and proper training to the teen and the supervisor. Supervisors have the greatest opportunity to influence teen work habits and prevent work injuries.

Historical Fact: The first state child labor law passed in 1836 when Massachusetts required children under age 15 working in factories to attend school at least 3 months per year. Six years later, Massachusetts limited children’s work days to 10 hours.
Securing And Collecting An Asset Based Loan
By: Paul A. Greco

Whether you are looking for a line of credit to improve cash flow, a term loan to purchase new equipment, or you are a lender funding a loan to a rapidly expanding new business, the lending environment has changed dramatically in the past several years. Today’s lenders are more cautious and their due diligence, especially in regards to a borrower’s non real estate based assets, more demanding. Accordingly, it is not surprising that we are receiving many calls from borrowers and lenders alike questioning how lenders secure their interests in a borrower’s accounts receivable, inventory, machinery, equipment, intellectual property and other tangible and intangible assets. These assets are the lender’s collateral in many asset based loans. This article will provide the lender and the borrower a working knowledge of how this type of collateral is collateralized and, in the event of a default, collected.

In an asset based loan transaction, the lender secures its rights in the collateral by entering into a security agreement with the borrower. The security agreement grants to the lender the right, in the event of a default, to seize and sell the collateral to satisfy the debt. The lender places the world on notice of its lien against the collateral by filing with the secretary of state of the relevant jurisdiction a financing statement. The financing statement, like a mortgage recorded with a recorder of deeds, provides notice to third parties of the lender’s rights in connection with the collateral.

When a default occurs, a lender may accelerate the debt owed to it and exercise its rights under the security agreement, including seizing control of and selling the the collateral in accordance with the Uniform Commercial Code (the “UCC”). Significantly, the UCC permits this process to go forward without judicial supervision. Accordingly, if the collateral includes the borrower’s accounts receivable the lender may simply notify the borrower’s customers that future payments to the borrower must be made directly to the lender.

Often times however, the valuable collateral may be a piece of equipment, inventory or even a customer list. In these cases, the Lender must first gain possession of the collateral before it can conduct a sale. This may be challenging. Undoubtedly, the security agreement will require the borrower to surrender control of the collateral upon demand but if the borrower refuses the lender may then peacefully repossess the collateral. If attempts at peaceful repossession fail the lender will need to seek judicial intervention in a replevin action.

Once in control of the collateral the lender may conduct a sale. There are other options, but typically the sale is a public sale. A public sale is similar to a judicial sale of foreclosure real estate, and like such a sale, competitive bidding is required. The overriding principle for any sale of collateral is that it must be conducted in a commercially reasonable manner. To accomplish this, strict adherence to the requirements of the UCC is essential. Minimally, notice of the sale must be given to the borrower, other lien holders and any guarantors of the loan. The sale must also be advertised in a manner that is likely to generate interest amongst the members of the public likely to purchase the collateral. This includes advertising the date, time and place of the sale in appropriate trade journals or other publications.

The successful bidder at the sale (who can be the lender) will receive title to the property free of all liens inferior to the lien of the party conducting the sale. The sale proceeds are applied to pay the costs associated with the sale, including attorney’s fees and selling commissions. The remainder of the sales proceeds is applied to the loan and any subordinate debts with the surplus, if any, being returned to the borrower. Notably, the sale does not have to be approved in any judicial process and upon the conclusion of the sale the borrower has no right to redeem the collateral.

A sale conducted in accordance with a security agreement and the UCC generally cannot be reversed. However, if the sale was not conducted in a commercially reasonable manner the borrower may be entitled to a money judgment against the lender and/or the lender may jeopardize its right to a deficiency judgment against the borrower and any guarantors.

Securing and collecting an asset based loan requires the lender to understand and stay informed about the borrower’s business and the borrower to be capable of presenting a clear and concise picture of its operations. Each transaction is unique and upon default each collection will have its own challenges. When in doubt about whether you are giving too much control to the lender or if a lien against the intended collateral is being properly perfected you should seek legal advice. However, the general considerations detailed above do provide both the borrower and the lender the perspective to begin discussions about an asset based loan.

Penalties to be Assessed on Late S-Corporation Tax Returns
By: Lin Hanson

Beginning in 2011, S-Corporations that file a late or incomplete Federal income tax return (Form 1120-S) will be assessed a penalty of $195 per shareholder per month. Husbands and wives are counted as two shareholders. For a 10-shareholder S-Corporation that is one year behind in filing its tax return, the penalty that may be imposed would be $23,400 (12 months x 10 shareholders x $195).
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