Felhaber Larson Fenlon & Vogt
A Professional Association – Attorneys at Law

BUSINESS REPORT

Issue 25 Spring 2007

Published by the law firm of Felhaber, Larson, Fenlon and Vogt, P.A.

DEFERRED COMPENSATION 2007 DEADLINE SECTION 409A AND SEPARATION AGREEMENTS

What is 409A?

Internal Revenue Code Section 409A was added in 2004 to require that a wide variety of deferred compensation arrangements be more specifically written to control an executive's ability to manipulate income tax deferral. It also restricts the prompt payout of deferred compensation to certain executives of publicly traded companies.

Authority

The statute was broadly written to cover a wide range of situations starting in 2005. The IRS' delay in releasing required guidance resulted in 2005 and 2006 generally being transition years to eventually comply with 409A.

Final Regulations released in April, 2007 clarify that December 31, 2007 is the final deadline for amending existing plans to comply with 409A.

Arrangements Covered

- Salary and bonus deferral arrangements
- Supplemental Executive Retirement plans ("SERPs")
- Discounted non-statutory stock option
- One person arrangements even if that person is not an employee (a service provider)

Separation Agreements

A. Two Times/Two-Year Safe Harbor
Involuntary Separation Agreements where the total payment does not exceed the lesser of two times (i) the qualified Plan annual limit (e.g. 2007, $225,000), or (ii) the employee's average annual salary, are exempt from the application of Section 409A if the payments are completed by no later than the end of the second calendar year following the year in which the employee separates from service.

B. Collectively Bargained Plans
Severance payments made as a result of collective bargaining agreements are currently exempt from Section 409A.

C. Short Term Deferral
Amounts paid within two and one-half months after the calendar year in which the right to payment has vested are not subject to Section 409A.

D. Reimbursement of Expenses
Reimbursements or direct payment by the employer of the participant's reasonable business, out placement or moving expenses or unreimbursed non-taxable medical expenses within limited

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BUSINESS CO-OWNERS: BUY-SELL AGREEMENTS

"Buy Sell" Agreements are very important documents that may have a variety of different forms. They are often somewhat neglected in the housekeeping of corporations, partnerships, limited liability companies, and other entities. In many instances, they control the disposition and valuation of the majority of a small business owner's assets, hence they are very important. Typically, a good deal of thought is required to prepare such agreements and have them properly executed. For example, often there are several business owners or associates, each of whom has a unique personal financial position, and a different time horizon for their active business career. Some may be employees of the company, and some may be passive investors, so attempting to take account of their mix of objectives and concerns in one document is a challenge. On the other hand, doing nothing and leaving it to chance is much too risky.

Very often the typical triggering events for a Buy-Sell transaction are premature death, long term disability, marital dissolution, debtor/creditor problems, voluntary and involuntary termination of employment. Some of these events are capable of being funded, or partially funded. For example, we often have fully funded life insurance buy out agreements in the event of premature death and we have disability buy out agreements that are funded with appropriate disability policies. Obviously, a number of the other trigger events are not capable of being funded through third party sources. Hence, such other events may require going to the bank to secure funds, or there may be a purchase money deferred sales agreement within the organization itself, or some other type of deferred funding. This funding aspect is generally very difficult. In many instances, the last thing you want is for your business associate to become your creditor. In some cases, lack of Buy-Sell funding can virtually bring a business to its knees. Many businesses begin at a modest level but over time grow to be very successful so as to require substantial funding. Thus, a good deal of planning is needed in this area.

Some types of entities may require more care than others. For example, professional associations require great care because there must be absolute compliance with the ethical laws of the profession and certain other statutory provisions must be met. You have to recognize that these professionals are both owners and workers. Consequently, in a small medical practice, if one of the primary physicians left, this would create two problems, the first of which is how to buy them out and the second is how to replace them as a key person in the organization without loss of patients and employees?

Subchapter S corporations also require some special planning because of the characterization of the entity.

Partnership relationships require some special considerations because of tax and other special characteristics of partnerships under partnership law. The same goes for limited liability companies.

Family businesses require special attention because you have a mixed situation with a family and a business. Finding a way to separate the two is very difficult. Also, very often in family business situations some of the persons are active in the management and some are passive owners in the business, which can create tensions between the two groups. Succession of leadership is very difficult.

Buy-Sells are very significant agreements which in many cases do not get the attention they need at the inception of the business. Too often as things progress and business grows, the owners are distracted and too often fail to give the Buy-Sell the attention it deserves.

Consequently, over the years we have seen substantial litigation in this area for the reasons discussed above as it relates to the fact that in many cases a large portion of one's balance sheet is controlled by a buy sell agreement and the persons involved have different objectives, needs, or wants.

In addition to the basic issues above, the Buy-Sell involves significant valuation, income, estate, and gift tax issues which are beyond the scope of this article.

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CHOOSING A TRADEMARK: WORD MARKS V. PICTURE MARKS

Agruably the strongest type of trademark registration from a legal standpoint is a "word mark", meaning a standard character trademark registration that is not restricted to any particular font or style.

Such a registration prevents others from using that same word in a confusingly similar way for a related product or service.

In contrast, a "picture mark" registration composed of a word or words in stylized letters, or a word or words combined with some graphic element, protects only the particular "look" that is registered. Such a registration does not preclude others from adopting a mark using the same words with a distinctly different look.

Some examples may be helpful.

A picture mark had been registered in 1979 as serial # 73210374, Reg. # 1142754, to cover the composite mark shown here:

This picture mark, above, would not necessarily prevent other meat companies from using the word SKYLARK.

But later the standard character mark "SKYLARK" was registered for meat products on August 8, 2000 as serial #75824356, Reg. #2375452. This standard character mark would prevent other meat companies from using the word "Skylark" in any form.

It should be noted however that other companies could use the term "Skylark" in trademarks for products unrelated to meat. Thus, Buick could name a car model the "Skylark". In addition there could be "Skylark" sunglasses or "Skylark" mattresses, because those uses are not likely to confuse consumers. No one is likely to think that a meat company is making cars, sunglasses or mattresses.

From the foregoing it should be obvious that the legal strength of a standard character mark is far greater than a picture or composite mark. Ideally then when choosing a new trademark you should seek to adopt a trademark which you can register in standard characters. Avoid merely descriptive or generic terms. Federal law does not permit the registration of trademarks on the Principal Register of terms that are "merely descriptive" or generic. Thus, Jolly Time might be a good popcorn trademark but "Butter Popcorn" would not be a valid mark. Similarly Totino's Pizza is a good mark but "Thin Crust Pizza" is too descriptive to be a trademark. Laudatory terms such as "WORLD'S BEST" Pizza also do not work as trademarks.

Note however that a generic term in stylized print, especially combined with some design element can serve as a mark and be registered. One example of such a registration is the following "picture mark":

CONSTRUCT-A-CLOSET

Geographically deceptive or misdescriptive marks should also be avoided. Thus, for a steakhouse restaurant located in Indiana and Illinois, when the beef served does not come from Colorado, you cannot register the trademark "The COLORADO Steakhouse" for the chain of restaurants. Nor can you register the trademark "NEW ENGLAND" for baked goods that are actually made in Minnesota. The same is true for the trademark MIDWEST FARMS for milk that does not come from the Midwest.

Before investing significant sums in establishing a new brand or trademark it is advisable to do a trademark search to be sure someone else is not already using a confusingly similar mark. We can assist you with such a search and help you evaluate potential trademarks.

Please contact Jim Blomquist for more information. Mr. Blomquist is located in our Minneapolis office.

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LOSS OF LAPTOP COULD BE A LEGAL PAIN

A client recently contacted us upset that his computer repair shop had lost his laptop containing account information for over 500 patients. He had an urgent problem under Minnesota law.

Do you or your employees have a computer that contains personal information about patients, customers, or clients? Minnesota law defines "personal information" as being names, combined with either account number, credit card number, social security number or driver license number.

In 2005, following numerous news stories about lost computers containing personal information, 20 states, including Minnesota, enacted laws requiring notice to affected individuals when their personal data has been compromised by a breach of security.

The Minnesota Statute is found at Section 325E.61.

If a business or person conducting business in Minnesota owns or licenses "personal information" of Minnesota residents then there is a duty under the law in the event of any breach in security if the data is either acquired by an unauthorized person, or is reasonably believed to have been acquired by an unauthorized person. Your duty is to immediately give notice. You must act "in the most expedient time possible", without unreasonable delay.

Action within 48 hours is also required to notify all nationwide consumer credit bureaus if the security breach involved over 500 persons. Such notice is to contain the timing, distribution, and content of the notices sent to affected persons.

Medical and dental practitioners please note that this law affects you.

As originally enacted the law contained an exemption for entities subject to HIPAA. That provision was changed and the law now exempts only financial institutions as defined in federal law.

Also, as originally enacted, the law did not apply if the data was encrypted. That provision was modified to allow for encryption or other "method of technology that makes electronic data unreadable or unusable", **unless** the encryption key, password, or other means necessary for reading or using the data was also acquired.

In view of this law it would be advisable to utilize passwords and encryption software. You should also adopt policies and procedures regarding use of passwords and protection of personal information held by a business and its employees. Let us know if we can help you.

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2007 Complimentary Seminars

Mark your calendars so you can attend our upcoming seminars, with discussions on a variety of timely legal topics. Seminars are free of charge, and include a complimentary breakfast and/or luncheon.

Business & Corporate Law	**Wed., Oct. 24th**	**Town & Country Club - St. Paul**
Builder Developer	**Thurs., Nov. 1st**	**Town & Country Club - St. Paul**
Labor & Employment Law	**Fri., Nov. 9th**	**Marriott Mall of America - Bloomington**

To receive a seminar invitation, email kdyck@felhaber.com. State your name and the name of the seminar(s) you wish to attend. Log on to **www.felhaber.com** for more information.

Felhaber Hires New Attorneys & Paralegals

Felhaber Larson Fenlon & Vogt is pleased to announce the addition of the following attorneys and paralegals:

Ms. Nauni Jo Manty's practice focuses on commercial litigation and complex bankruptcy matters. She has represented creditors in all types of settings from enforcing creditors rights and remedies in state court as well as in federal court. Most recently, she represented the City of Duluth, Duluth Economic Development Authority and the Duluth Airport Authority in the Northwest Airlines bankruptcy. She also serves as a Chapter 7 panel trustee, has served as a Chapter 11 trustee and is a Court-appointed receiver in a Securities Exchange Commission matter in U.S. District Court.

Ms. Julie Boemke and **Ms. Nancy Jaeckels** have also joined Felhaber. They both serve as Trustee Administrators, and work with Ms. Manty. You may contact Ms. Manty and her support team at the Minneapolis Office.

Ms. Barbara Kristiansson practices primarily in the areas of estate planning and probate. Prior to joining Felhaber, Ms. Kristiansson worked in the areas of accounting, estate tax, and estate settlement. You may contact Ms. Kristiansson at the St Paul Office.

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Governor Tim Pawlenty Appoints Jon Hopeman to The Board on Judicial Standards

Governor Tim Pawlenty appointed Felhaber Attorney Jon Hopeman to The Board on Judicial Standards. The Board on Judicial Standards investigates allegations of misconduct by Minnesota judges and referees and recommends discipline to the Minnesota Supreme Court, including censure, suspension, retirement or removal of judges. The board consists of 10 members appointed by the Governor, including one judge of the Court of Appeals, three trial court judges, two attorneys with at least 10 years of experience in the state and four public members.

Jon Hopeman

periods following the separation from service are exempt from the application of Section 409A.

E. De Minimis

All payments, reimbursements and benefits under a separation pay arrangement that do not exceed $15,500 (for 2007), are not subject to 409A.

Sanctions for Violating 409A

The employee is hit with an additional 20% income tax penalty on any payments from plans that are not 409A compliant.

For more information contact Tom Hughes or Ruth Marcott.

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Business Report

The Business Report is an update on legal developments. It is not intended to be legal advice and should not be relied upon without consulting counsel.

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