

31st Annual Tax Symposium

ALLOCATION OF PURCHASE PRICE

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- I. ALLOCATIONS TO REDUCE INCOME TAX IN AN ASSET SALE WHEN SELLER IS A "C" CORPORATION
 - A. Allocate to personal goodwill ("PG")
 - B. Allocate to covenant not to compete ("Covenant")
- II. IRC §1060: APPLICABLE ASSET ACQUISITION
 - A. Assets constitute a trade or business; and
 - B. The transferee's basis is determined wholly by reference to the consideration paid for the assets
- III. IRS FORM 8594 "ASSET ACQUISITION STATEMENT UNDER SECTION 1060"
 - A. Must be filed by purchaser and seller
 - B. Must be filed in the year of the sale
 - C. Requires disclosure of a Covenant, lease, employment agreement or similar arrangement to which a **shareholder** and the purchaser are parties, i.e., a transaction outside of the asset purchase agreement. (See Part II, Question 6)
 - D. Does not require disclosure of make up of Class V or Class VI assets
 - E. Classes of Assets, Part II of Form 8594.
 1. Cash
 2. Actively Traded Personal Property
 3. Assets the Taxpayer Marks to Market
 4. Inventory

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5. Assets other than 1, 2, 3, 4, 6 and 7 e.g.: furniture, fixtures, building, land, vehicles and equipment
6. §197 intangibles
 - Workplace in force
 - Business books and records
 - Customer based intangibles
 - Supplier based intangibles
 - License and permits
 - Know how; formula etc.
 - Agreements not to compete
7. Goodwill and Going Concern Value

IV. FACTORS THAT SUPPORT THE EXISTENCE OF PG

1. Discussion of allocation in letter of intent and asset purchase agreement
2. Buyer requires shareholder to sign a noncompete
3. Seller is named after shareholder
4. Shareholder is recognized in the industry or community
5. Customers and suppliers deal with the shareholder
6. Shareholder is engaged with seller on a full-time basis

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V. FACTORS THAT NEGATE THE EXISTENCE OF PG

1. Shareholder has signed a Covenant with seller
2. Discussion regarding allocation to PG is an afterthought
3. Other employees of seller are engaged in sales and have customer relationships
4. Seller serves customers without participation of shareholder

VI. GENERAL COMMENTS

- A. A "C" corporation is taxed at ordinary income rates – not capital gain.
- B. A bonus to the president (shareholder of seller will reduce income in the year of sale) but the amount is limited by IRC Section 162 – ordinary and necessary business expense.
- C. Retain a consultant to value the PG. Two-step process:
 - i. Establish that there is PG
 - ii. Value the PG
- D. Use of separate agreements for:
 - i. Sale of PG
 - ii. Covenant
- E. Purchaser may not care about allocation because any intangible is a Section 197 intangible amortized over 15 years.

Attachment: - IRS Form 8594

**Asset Acquisition Statement
 Under Section 1060**

OMB No. 1545-0074

▶ Attach to your income tax return.

Attachment
 Sequence No. **169**

▶ Go to www.irs.gov/Form8594 for instructions and the latest information.

| | |
|-------------------------|---------------------------------------|
| Name as shown on return | Identifying number as shown on return |
|-------------------------|---------------------------------------|

Check the box that identifies you:
 Purchaser Seller

Part I General Information

| | |
|--|----------------------------------|
| 1 Name of other party to the transaction | Other party's identifying number |
|--|----------------------------------|

Address (number, street, and room or suite no.)

City or town, state, and ZIP code

| | |
|----------------|-------------------------------------|
| 2 Date of sale | 3 Total sales price (consideration) |
|----------------|-------------------------------------|

Part II Original Statement of Assets Transferred

| 4 Assets | Aggregate fair market value (actual amount for Class I) | Allocation of sales price |
|------------------|---|---------------------------|
| Class I | \$ | \$ |
| Class II | \$ | \$ |
| Class III | \$ | \$ |
| Class IV | \$ | \$ |
| Class V | \$ | \$ |
| Class VI and VII | \$ | \$ |
| Total | \$ | \$ |

5 Did the purchaser and seller provide for an allocation of the sales price in the sales contract or in another written document signed by both parties? Yes No

If "Yes," are the aggregate fair market values (FMV) listed for each of asset Classes I, II, III, IV, V, VI, and VII the amounts agreed upon in your sales contract or in a separate written document? Yes No

6 In the purchase of the group of assets (or stock), did the purchaser also purchase a license or a covenant not to compete, or enter into a lease agreement, employment contract, management contract, or similar arrangement with the seller (or managers, directors, owners, or employees of the seller)? Yes No

If "Yes," attach a statement that specifies (a) the type of agreement and (b) the maximum amount of consideration (not including interest) paid or to be paid under the agreement. See instructions.

Part III Supplemental Statement—Complete only if amending an original statement or previously filed supplemental statement because of an increase or decrease in consideration. See instructions.

7 Tax year and tax return form number with which the original Form 8594 and any supplemental statements were filed.

| 8 Assets | Allocation of sales price as previously reported | Increase or (decrease) | Redetermined allocation of sales price |
|------------------|--|------------------------|--|
| Class I | \$ | \$ | \$ |
| Class II | \$ | \$ | \$ |
| Class III | \$ | \$ | \$ |
| Class IV | \$ | \$ | \$ |
| Class V | \$ | \$ | \$ |
| Class VI and VII | \$ | \$ | \$ |
| Total | \$ | | \$ |

9 Reason(s) for increase or decrease. Attach additional sheets if more space is needed.
