VOLUME 7

FINEMAN & BACH, P.C.

SPRING 2001

LEGALNOTES

INFORMATION FOR OUR BUSINESS AND CORPORATE CLIENTS

IN THIS ISSUE

Can College Savings Plans Help You?
Page 1

Eight Ways to Reduce Your Risk of Loss and Help Avoid Costly Litigation
Page 2

Make Sure Your Non-Compete Agreements are Enforceable
Page 3

Updated E-Mail Addresses
Page 4

FINEMAN & BACH, P.C.
1608 Walnut Street
19th Floor
Philadelphia, PA 19103
(215) 893-9300
Facsimile: (215) 893-8719

New Jersey Address:
Fineman & Bach
3 South Haddon Ave.
Haddonfield, NJ 08033
(856) 795-1118
Facsimile: (856) 795-1110

www.finemanbach.com

The material in this newsletter is general information for clients and friends of Fineman & Bach, P.C., and it is not intended to be used for any other purpose. For legal advice or answers to specific questions, please contact one of our attorneys.

Can College Savings Plans Help You?

College costs have increased dramatically over the last 20 years. To help families fund the cost of a college education, the federal government has sanctioned the establishment of qualified state tuition programs that provide tax-favored treatment. These college savings plans are commonly called Section 529 Plans after the Internal Revenue Section that allows them.

Two Types of Programs

Qualified state programs come in two varieties: Prepaid Tuition Plans and College Savings Plans. Prepaid Tuition Plans are essentially state operated trusts, designed to provide a hedge against tuition inflation. Pennsylvania's plan is called the Tuition Account Program or "TAP", and is one of the better examples of this type of plan. Under the TAP Plan, you can buy blocks of college credit hours, using today's cost of a public or private university, either in or out of state. For instance, if you paid $5,000 today and bought one semester credit at a private university, and 20 years from now, that same one semester's credit would be worth $15,000, your TAP credit would pay the $15,000 cost.

College Savings Plan offers more flexibility. With this plan, you invest money with the state that is typically managed by a large mutual fund company. Here, the risk is an investment risk. The account may grow faster or slower than the increase in tuition costs or may suffer a reduction in the principal.

Tax Benefits of Section 529 Plans

Tax benefits under either a Prepaid Tuition or a College Savings Plan are as follows:

- Contributions are not tax deductible, but income tax on the earnings are deferred until they are withdrawn, at ordinary income tax rates.
- The tax on the earnings is calculated based on the tax rate of the beneficiary (the student) rather than the rate of the account's owner (the parent or grandparent). This is advantageous since students are usually in a lower tax bracket. However, the withdrawal must be used to pay for eligible higher education expenses such as tuition, books, supplies and room and board expenses at an eligible educational institution. Each state's program may provide a different definition of eligible expenses.
- If funds are withdrawn and not used for an eligible expense, the earnings are taxed to the distribution recipient. There is also a penalty equal to at least 10% of the earnings that were used for non-qualified purposes. Most states allow the designated beneficiary of one of these plans to be changed to another family member, at any time. So, if one child does not use up the fund, the balance may be transferred to another child.
- The Section 529 Plan receives a favorable estate tax treatment since the value

(continued on page 4)

Eight Ways to Reduce Your Risk of Loss and Help Avoid Costly Litigation

The old expression that an ounce of prevention is worth a pound of cure, certainly is holds true in today's complex business environment. To blindly assume that litigation can not happen to you is to play a form of business "Russian roulette". However there are some simple steps that a business person can take to reduce the risk of litigation.

1. Make certain that your lease really protects you.

To protect yourself, make certain that your lease, as much as possible, shifts the risk of loss to your tenant. The lease should also require your tenant to indemnify you for any third party claims arising out of your tenant's business. The indemnity provision should require your tenant to pay any attorneys fees you might incur defending the claim.

2. Make certain that your commercial tenant names you as an additional insured.

Most leases require your commercial tenant to name you as an additional insured on the tenant's insurance policy. When litigation occurs, an owner often discovers that the tenant has failed to fulfill this obligation and the owner must retain his or her own counsel. To prevent this oversight from occurring, require your tenant to provide you an endorsement naming you as an insured at the signing of the lease and each time the insured's policy is renewed.. Do not accept a certificate of insurance issued to you as proof that your are insured under your tenant's policy. A certificate of insurance merely states that the tenant is insured with a particular company.

3. Take reasonable steps to insure the safety of your customers.

The law requires that you take reasonable steps to insure the safety of your customers. This legal duty can be satisfied by conducting regular inspections of your property and taking immediate steps to correct any defects or dangerous conditions. It is extremely helpful to maintain a written log which lists the time and the signature of the employee who conducted the inspection.

4. Train your employees to respond promptly and courteously.

In a study of why patients sued their physicians for medical malpractice, many plaintiffs stated that the dispute could have been avoided if their physicians had taken the time to fully explain their diagnosis and treatment. This study highlights a lesson that we can all apply in our daily business practices. A quick response to a dissatisfied or injured customer, can be the difference between maintaining a business relationship or becoming adversaries in the courtroom. Train your employees to respond promptly and courteously to these situations and you might be able to avoid any difficulties later.

5. Contact your lawyer.

If you believe that you are facing a potential claim, contact your lawyer. Together you can develop a quick response and possible avoid expensive litigation down the road. Ultimately, this ounce of prevention will serve you well.

6. Contact your insurance company, if you think you have a claim.

If, despite your best efforts, you are facing a situation that you believe might result in a claim, contact your insurance company. Your insurance company employs trained professionals who are experienced in handling claims. By failing to notify the carrier, you deprive your insurer of the opportunity to resolve the situation before it develops into a lawsuit.

7. Document, Document!

Some of the largest jury verdicts involve employment disputes. Employees sue employers claiming that they have been wrongfully terminated. By taking some basic measures, you can limit your exposure if you should be involved in an employment dispute. Employee handbooks detailing company policies can be very important evidence of your business practices. However, the handbook is of little value if it is not kept current and not provided to each employee. Make each employee sign an acknowledgment that he or she received the handbook at the time of hiring or whenever the handbook is revised. If you do written evaluations of your employees, have the employee sign the evaluation acknowledging that he or she read the evaluation, discussed the evaluation and agreed with the evaluation. If the employee disagrees with the evaluation, have that employee explain, in writing, why he or she disagrees. When you conduct your employee reviews always have a witness to avoid the "he said, she said" situation.

8. Conduct annual risk assessments.

Annually, you must take the time to review your business practices to make certain you are taking the necessary steps to limit your exposure to future litigation. Taking the time to sit down with your lawyer, insurance professional and risk manager will ensure that you are not overlooking any important steps that you can take to avoid costly disputes.

Following these simple steps can make those words in the old proverb ring true!

For more information, contact
Jay Barry Harris E-mail
at (215) 893-8704

Make Sure Your Non-Compete Agreements are Enforceable

Most employers realize that a valid agreement is required if you want to limit an employee's use of customer lists, confidential information or trade secrets when the employee leaves your company. Such agreements are commonly called "non-compete" agreements, or "restrictive covenants." Courts will not enforce every agreement. It pays to have your employee agreements reviewed by counsel before you have them signed.

Courts in Pennsylvania have interpreted agreements which limit an employee's ability to compete in a variety of ways. It is extremely important that the agreement be carefully drafted to ensure that it will stand up in court. Here are some of the common pitfalls to avoid:

- Timing is critical when it comes to signing an agreement not to compete. There must be consideration for the restrictive covenant. Courts have held that the agreement must be signed at the time employment commences; if not, there must be adequate additional consideration. Courts have also interpreted this requirement to mean that if a restrictive covenant is not executed simultaneously with the initial taking of employment, the covenant will not be enforced unless the employee receives a corresponding benefit or change in status. An employee's continued employment is not sufficient consideration for a covenant not to compete which the employee signs after the inception date of his employment. What does this mean to you? If you wish an existing employee to now sign a covenant not to compete, review the situation with your counsel to insure that the agreement is likely to be upheld.
- Overly broad agreements will not be upheld. The agreement not to compete must be reasonably limited in terms of activity, time and geography. The key word is "reasonable." Courts will look at each contract on a case by case basis, and will ask whether an agreement that limits a former employee from engaging in certain activities, over a certain period of time, in a certain geographical area, makes sense, or is oppressive to the employee. The definition of what is "reasonable" will vary widely depending upon the industry involved. For example, a court found that a three year limitation upon a salesman who sells products to the cable television industry was unreasonable, and the court refused to enforce it. In that case, the court believed that the agreement was intended to "enslave" the employee to the employer for three years. In order to avoid a similar outcome, make sure the terms of your agreement are reviewed and are enforceable.
- Courts also require the agreement to be "reasonably necessary" to protect legitimate interests of the employer. In some situations, the courts will "reform" an agreement and will impose terms that the court feels are appropriate. However, if your agreement is too over-reaching, a court may simply decline to enforce it at all. In the example of the cable television salesman above, the court found the agreement to be so "severely overbroad as to evince an intent to oppress defendant." Accordingly, the court ruled that the covenant cannot be reformed, and the employer was left with no remedy.

Therefore, when your legitimate business interests do require you to limit an employee's ability to compete with your company when the employee leaves, it makes sense to have an attorney assist in the drafting of an agreement that will be upheld in court. Get legal advice before the agreement is signed to make sure that there is adequate consideration for the agreement. If the agreement is not being signed at the inception of employment, it is necessary to provide adequate consideration to the employee.

Don't try to impose an unreasonable agreement upon an employee with the expectation that the court will reform the terms if the agreement goes too far. A court may decline to do so. A better approach is to have an agreement drafted that is appropriate to your industry and to the employee in question. In this manner, you can be assured that a court will not view your covenant not to compete as oppressive, and your interests will be protected.

For more information contact
Diane Bernoff Sher E-mail
at 215-893-8726

(continued from page 1)

Can College Savings Plans Help You?

of the account is removed from the owner's estate. However, if the beneficiary dies, the value of the account is part of the beneficiary's taxable estate.

- The tax code imposes no specific dollar contribution limits on aggregate contributions for these qualified plans, but requires adequate safeguards for contributions that exceed what the beneficiary may need for his or her education expense. States vary on contribution limits.
- Contributions to the plan receive favorable gift tax treatment. They qualify for the $10,000 annual gift tax exclusion and the generation skipping transfer tax exclusion. In addition, the donor can make a special election that allows him to treat the contribution as if it were made over five years. This enables the donor to contribute up to $50,000 per person in the initial year to a beneficiary's account, and have it treated as though it were made over five years so that it qualifies for the annual gift tax exclusion. If a husband and wife join together in the gift, an initial contribution of $100,000 may be made.

Benefits and Drawbacks

The Section 529 Plan offers several advantages over other types of investment vehicles for saving for college. The main advantage is that you can front load the $10,000 annual gift tax inclusion by placing $50,000 per person in the Section 529 Plan without triggering a gift tax, and allow these funds to grow income tax free. Another advantage is that there are fewer ongoing administrative requirements for a Section 529 Plan as compared to a trust which requires annual tax returns and notices of contribution.

However, despite these attractive features, a more traditional college savings vehicle, the "Crummy Trust" offers certain benefits that the Section 529 Plan cannot duplicate. For instance, a major disadvantage of Section 529 Plans is that there is a lack of investment discretion given to the donor over the funds. The donor will rely upon either the state or a mutual fund for management of the fund. With a Crummy Trust, the trustee can invest the funds as the trustee may determine. In addition, a Crummy Trust created to handle funds for college can have more flexibility in disbursements or retaining funds depending on the beneficiary's age or accomplishments. A Crummy Trust can also handle more unusual investments, like an interest in a family limited partnership or closely held business.

In Section 529 Plans, gains on the investment are converted from capital gain to ordinary income. For wealthy grandparents, the use of a Section 529 Plan is a waste of their annual gift tax exclusion because education payments for grandchildren (if made to the college or school directly) do not use up the grandparents' annual gift tax exclusion.

The Choice Depends On Your Circumstances.

The Section 529 Plans are very impressive in terms of the benefits that they offer, especially for parents who want to begin saving early for their children's college education. Some tuition plans are more beneficial to residents than nonresidents in that the income may be tax free when withdrawn for state income tax purposes. Some plans offer lower management fees, higher contribution limits, asset allocation strategies or the ability to move funds from one beneficiary to another. Depending on the circumstances, such as the amount and frequency of the investment you wish to make; and the powers you wish to retain, a trust may be a better alternative.

For more information, contact
Scott H. Mustin, Esquire E-mail
at (215) 893-8741.

Please note our E-mail addresses:

S. David Fineman
sdfineman@finemanbach.com

Mitchell L. Bach
mbach@finemanbach.com

Lee Applebaum
lapplebaum@finemanbach.com

Norman S. Berson
nberson@finemanbach.com

Richard C. DeMarco
rdemarco@finemanbach.com

Phinorice B. Dixon
pdixon@finemanbach.com

Drew S. Dorfman
ddorfman@finemanbach.com

June J. Essis
jessis@finemanbach.com

Krista Frankina Fiore
kfiore@finemanbach.com

Kerri J. Fleming
kfleming@finemanbach.com

Michael F. Frisbie
mfrisbie@finemanbach.com

Jay Barry Harris
jharris@finemanbach.com

Sheldon Kivell
skivell@finemanbach.com

Robert A. Klein
rklein@finemanbach.com

Michael H. Krekstein
mkrekstein@finemanbach.com

Gary A. Krimstock
gkrimstock@finemanbach.com

Scott H.Mustin
smustin@finemanbach.com

Richard A. Perr
rperr@finemanbach.com

Richard A. Rubin
rrubin@finemanbach.com

Michael S. Saltzman
msaltzman@finemanbach.com

Diane Bernoff Sher
dbsher@finemanbach.com

Vickie Simon
vsimon@finemanbach.com

Carl F. Staiger
cstaiger@finemanbach.com

Carol A. Tino
ctino@finemanbach.com

David R. White, Jr.
dwhite@finemanbach.com