Manufacturer

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Creative ways for manufacturers to attract fresh talent

Naive young people may not think factories are the most glamorous places to work. But owners of manufacturing companies know firsthand just how rewarding careers in this sector can be, both financially and intellectually. Some have found creative ways to breathe new life into their mature companies by enticing millennials — roughly defined as people born between 1980 and 2000 — to join their workforces.

Offer value-added work environments

Millennials tend to be more technology savvy and innovative than previous generations, according to executive feedback reported in the 2014 Duke University / *CFO Magazine* Global Business Outlook Survey. Hiring workers with such attributes can give a manufacturer the creative edge it needs to outmaneuver competitors.

As an added bonus, younger workers tend to have lower salary expectations and value nonmonetary perks and benefits over cash. In fact, 45% of millennials prefer flexible work environments over pay, according to "The Cost of Millennial Retention," a report published by research and consulting firm Millennial Branding and the career network Beyond.com. They want to choose when and where they work, rather than working traditional 9-to-5 jobs. Many young people also seek careers that provide a sense of personal fulfillment.

Many businesses and schools work together in Project Lead the Way programs that start preparing students for science, technology, engineering and math careers as early as kindergarten.

Examples of offerings that appeal to millennials include flextime arrangements, mentoring programs, and additional training and licensing opportunities. For example, a millennial worker may be incentivized by a year end bonus program that's based on developing innovative solutions to lower costs and waste (lean manufacturing) or improve product quality (Six Sigma principles).

Stay ahead of the technology curve

Technology is an important part of the daily life of millennials — and they know how to use it to improve efficiency. Millennials are also likely to try to integrate intuitive devices and online services used in their personal lives into the workplace, such as tablets, video chat, social media and cloud computing.

Managers can leverage millennials' deep understanding of technology by involving them in purchasing decisions. Some forward-thinking manufacturers have even added millennials to their boards of directors to increase diversity and offer fresh, technology-driven perspectives on such issues as strategic investment decisions and data security.

Distributors feel their own labor pains

Distribution companies are having trouble attracting and retaining reliable, experienced truck drivers, according to the American Trucking Associations (ATA). Last year, the average annualized driver turnover rate rose for both large truckload carriers and less-than-truckload companies. Although the driver shortage isn't as dire as it was during the early 2000s, it's expected to worsen as the economy heats up, regulatory oversight increases and baby boomer drivers continue to retire.

For distributors with trucking fleets, this trend underscores the importance of offering drivers competitive wages and benefits. If you're curious how your compensation packages measure up, the ATA released the results of a compensation study last December that revealed the median pay for drivers ranged from $46,000 for national, irregular route dry van truckload drivers to $73,000 for private fleet van drivers — and about 80% of truckload fleets offer paid holidays. The most common payment method was mileage-based, but three out of four fleets also pay hourly rates to some drivers. About 80% of private carriers offer 401(k) retirement plans and match employee contributions.

There's more to compensation than just money, however. Trucking companies of all sizes that provide friendly, safe, flexible and low-stress work environments may have the edge needed to attract and retain younger drivers.

Recruit and mentor

So how do you attract millennials to your workplace? Young people today face a tighter job market compared to previous generations. But there's an ongoing talent gap in manufacturing, especially high-tech niches. Proactive high school and college academic advisors are often instrumental in directing students toward careers in high-demand manufacturing sectors and recommending apprentice or internship programs.

Many businesses and schools work together in Project Lead the Way (PLTW) programs that start preparing students for science, technology, engineering and math (STEM) careers as early as kindergarten. Today roughly 6,500 schools operate PLTW programs in all 50 states.

Manufacturing companies are a key partner in PLTW programs. For example, owners and managers may mentor students and teachers, companies may lend technology equipment to community colleges and high schools, and human resources departments may offer apprentice or internship programs.

Not only do PLTW programs offer opportunities for manufacturers to give back to local communities, but they also create a source of workers trained in STEM disciplines that they can draw from in the future. And money spent on these training programs may be deductible for income tax purposes — and, in some cases, may generate federal and state tax credits that could be refundable or carried forward to future periods.

Overcome stereotypes

Manufacturers and millennials can be a winning combination. But first manufacturers need to refresh the sector's image by promoting flexible work options and personal development opportunities, investing in millennial-friendly technology and participating in PLTW programs. Contact your financial advisor to brainstorm creative solutions and maximize the tax benefits of attracting and hiring millennials. ■

Should manufacturers consider the expired research tax credit?

Congress first approved the "temporary" research tax credit in 1981, and it's been renewed 17 times since, often retroactively to its prior expiration. On Dec. 31, 2014, the research credit expired yet again. The congressional track record of continually renewing this credit suggests that it'll be available again in 2015. To be prepared, manufacturers engaged in research activities should understand when and how to claim these credits. Even if the credit isn't extended, you might be able to save tax by filing amended returns to claim the credit for recent years.

4-factor test

To be eligible for the research credit (also commonly referred to as the "research and development" or "research and experimentation" credit), a business must have engaged in "qualified" research activities. To be considered "qualified," activities must meet the following four-factor test:

1. The purpose must be to create new (or improve existing) functionality, performance, reliability or quality of a product, process, technique, invention, formula or computer software that will be sold or used in your trade or business.
2. There must be an intention to eliminate uncertainty.
3. There must be a process of experimentation. In other words, there must be a trial and error process.
4. The process of experimentation must fundamentally rely on principles of physical or biological science, engineering or computer science.

Among those activities specifically excluded from the credit are reverse engineering an existing product, research related to social sciences, arts or humanities, software developed for internal use, and research performed outside the United States and its territories and possessions. Research that's funded or reimbursed by someone else via a contract, grant or other arrangement is also excluded.

Expenses that qualify for the credit include wages for time spent engaging in supporting, supervising or performing qualified research, supplies consumed in the process of experimentation, and 65% of any contracted outside research expenses.

Methods to compute your credit

There are three options for computing research credits:

Traditional method. Here you first compute qualified research expenses as a percentage of gross revenue for the period between 1984 through 1988. In turn, that historic fixed base percentage is multiplied by the average of the four prior years' gross revenue to determine the current base amount. The credit equals 20% of

the excess over that base amount. For example, if your current base amount is $100,000 and your qualified expenses are $150,000 for the current year, you're eligible for a $10,000 credit (20% of $150,000 - $100,000).

Keep in mind that amended returns may be filed to claim research credits up to three years back, potentially allowing you to reap refunds from previous years.

Start-up calculation method. This technique can be used if a company was founded after 1983 or had less than three years of activities between 1984 and 1988. It uses a historical build-up computation to establish the fixed base percentage and then, similar to the traditional method, allows a credit for 20% of the excess qualified research expenses.

Alternative simplified credit method. A company uses this option when it either cannot establish its historic fixed base percentage or that percentage is so high that the credit would be limited significantly. Here the fixed base is 50% of the average research expenses incurred in the previous three years and the credit is 14% of the excess. For example, if a manufacturer averaged $100,000 per year of qualified expenses over the last three years, the credit would be $7,000 (14% of $50,000) even if its research activities didn't increase.

Keep in mind that amended returns may be filed to claim research credits up to three years back, potentially allowing you to reap refunds from previous years.

Food for thought

Claiming research credits can be tricky. Alternative minimum tax issues could undermine your plans to use these credits. On the other hand, if your state also offers credits for research activities, the research credit may be even more significant than you initially anticipated. So discuss with your tax advisor whether it's worth pursuing — and for the latest on whether Congress extends it again for 2015. ■

Why deal structure counts

Comparing and contrasting asset and stock deals

The merger and acquisition market is picking up along with the performance of the manufacturing sector. Today's market is generally more seller-friendly than during the recession, when buyers were primarily trolling for distressed companies. Healthy, profitable companies can typically sell at higher pricing multiples today than five years ago, which means sellers don't necessarily have to concede to their buyers' every demand.

If you're planning to buy or sell corporate assets or stock, you'll need to negotiate more than just the selling price. How you structure the deal can have a major impact on how much cash and potential liabilities you'll wind up with after the dust settles.

Asset vs. stock sales

A fundamental choice in a corporate deal is whether its stock or its assets will be sold. In a stock sale, all the outstanding shares of stock transfer to the buyer, and the business can continue to operate uninterrupted.

Asset sales are more complex. The buyer purchases all (or most) of the corporation's assets and liabilities, renegotiates contracts and applies for new licenses, titles and permits.

From a tax and liability perspective, sellers generally prefer a stock sale, while buyers typically prefer an asset sale.

A seller's point of view

With a stock sale, sellers pay tax on the difference between the selling price and their basis in the stock — and at the more favorable long-term capital gains rate as long as they've held the stock for more than 12 months.

But asset sales trigger double taxation for C corporations. The shell corporation — which the seller retains and winds down in an asset sale — pays tax on the gains from selling assets. And the shareholders pay tax on cash distributions.

Asset sales also can leave sellers vulnerable to future lawsuits, such as employee discrimination or intellectual property claims. Another consideration is depreciation recapture — it's often overlooked even though it has the potential to significantly reduce the amount of cash taken away from the sale.

View from the buy-side

When buyers purchase stock, assets stay at book value, and existing depreciation schedules apply. Although simpler to execute, stock sales typically result in higher taxable income for the buyer than do asset sales. With a stock sale, the buyer may be vulnerable to future lawsuits and other legal claims.

Asset sales enable the buyer to report assets, such as equipment and furniture, at fair market value. The value allocated to each fixed asset provides a fresh basis for depreciation, thereby lowering taxable income in the future. Under this arrangement, the buyer can avoid certain legal claims associated with the seller's corporation.

S corp alternative

S corporations have a third option that may serve as a middle ground between asset and stock sales. By electing IRC Section 338, the parties may be eligible to treat a stock sale like an asset sale for federal tax purposes. Although the election won't save sellers any tax, buyers will reap the tax benefits of an asset sale.

To make a Sec. 338 election, the buyer and seller must sign and *jointly* file Form 8023. Then each must file Form 8883, which allocates the purchase price among seven categories of assets, including cash, inventory and goodwill. Some of these categories — for example, inventory — are taxed as ordinary income. Others are subject to a capital gains tax. So, this allocation has important tax consequences for the seller.

Outside perspectives

Asset and stock sales aren't something owners of manufacturing and distribution companies handle on a daily basis. When you decide to buy or sell, it's critical to structure the deal in the most advantageous way possible from both legal and financial perspectives. Attorneys and CPAs for both the buyer and seller should be intimately involved throughout the process to help you make informed choices. ■

Spotlight on financing alternatives

Private manufacturers and distributors can select from a wide menu of loan options from financial institutions. Popular choices include lines of credit, term loans, leases, mortgages and Small Business Administration (SBA) loans. Which is right for your business in today's low-interest, tight lending environment?

Lines of credit

You may need a line of credit to fund working capital shortages that arise as you grow or ramp up inventory during seasonal or cyclical peaks. These loans are usually based on the prime interest rate and collateralized by the company's accounts receivable and inventory.

Credit lines give borrowers open-ended access to cash, with flexible repayment terms and without the need to reapply every time there's a working capital shortage. However, banks reserve the right to review a borrower's financial statements and periodically readjust credit terms or call the line.

Term loans and leases

You may need equipment and vehicles to make goods or deliver them to customers. These fixed assets can either be purchased with cash and loan proceeds or be leased.

Purchasing fixed assets with term loans makes sense when you expect the items to last for a long time without becoming obsolete. Creditworthy businesses can usually borrow up to 80% of an asset's purchase price at a fixed interest rate over five to seven years.

Leasing may be a smart alternative when assets will need upgrades or you have limited capital for a down payment. Lease payments are typically lower than term loan payments, but the company doesn't own the equipment at the end of the lease term. Some banks offer hybrid products that combine the best elements of leasing and owning, however.

Mortgages

Banks also finance real estate purchases and construction projects. Commercial property mortgages typically require a loan-to-value ratio of 80% over a 15- to 20-year amortization.

Property ownership gives manufacturers more control over making improvements. Plus, manufacturers that build up equity in property can pledge it as additional collateral.

SBA loans

Commercial banks are the intermediary for loans that are guaranteed by the SBA. One popular option is the 7(a) program, which offers general purpose loans to small businesses (as defined by the SBA based on industry classification codes).

There are a few use restrictions. For example, proceeds can't be used to buy an asset to hold for its potential increased value or to reimburse owners for money they previously put into their business.

Ready, set, apply

Contact your financial advisor for more information on these banking options or for help compiling financial data to apply for a loan with confidence. ■

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