

## GLOSSARY OF TERMS

### **401(k) Plan**

401(k) plan is a type of profit sharing plan that allows employees to choose between receiving current compensation (and being taxed on it) or deferring compensation to a 401(k) plan (and deferring tax on it) through a "cash or deferred arrangement" (CODA). Employers frequently make a matching contribution equal to some percentage of the employee's elective salary deferral. A 401(k) plan can also provide for profit sharing contributions made by the employer and allocated to the accounts of all plan participants in a uniform, non-discriminatory manner. Plan participants are usually able to allocate their 401(k) contributions among the various investment alternatives available in the plan. The amount of a participant's retirement benefit is then based on the value of the participant's account at retirement.

### **403(b) Plan**

A tax-deferred annuity retirement plan available to employees of public schools and certain nonprofit organizations.

### **A/B Trust**

A type of Revocable Living Trust used by married couples. In this type of living trust, two trusts (trust A and trust B) are created at the time the first spouse dies. By dividing the couple's estate into two trusts at the first death, each spouse can pass the maximum amount of property allowed to avoid federal estate taxes. One trust, usually trust A, is often referred to as the marital deduction trust and the other trust, usually trust B, is often referred to as the shelter trust.

### **Adjusted Book Value**

The book value that results after one or more asset or liability amounts are added, deleted or changed from the respective book amounts.

### **Administrator**

The person designated by the court to manage and distribute a probate estate when there isn't a will. If there is a will, the person so designated is called the executor (male), executrix (female), or personal representative.

### **Advance Directive**

A general term that describes two kinds of legal documents, living wills and medical powers of attorney. These documents allow a person to give instructions about future medical care should he or she be unable to participate in medical decisions due to serious illness or

incapacity. Because each state regulates the use of advance directives differently, individuals need to obtain an advance directive in the state they currently reside.

### **Affiliated Services Group (AFG)**

A group consisting of a service organization joining two or more entities as a single employer for qualified plan purposes. An affiliated service group is a group of related employers and refers to two or more organizations that have a service relationship and, in some cases, an ownership relationship. An affiliated service group can fall into one of three categories:

1. A-Organization groups (referred to as "A-Org"), consists of an organization designated as a First Service Organization (FSO) and at least one "A organization"
2. B-Organization groups (referred to as "B-Org"), consists of a FSO and at least one "B organization"
3. Management groups.

### **Alternate Valuation Date**

A date exactly six months following the decedent's date of death. The personal representative may choose to utilize this date instead of the descendant's date of death only if it lowers the tax liability for the estate.

### **Ancillary Probate**

A probate proceeding conducted in a state other than the state where the decedent lived and the primary probate occurs.

### **Annual Exclusion**

The amount of property the IRS allows a person to gift to another person during a calendar year before a gift tax is assessed and/ or a gift tax return must be filed. The amount is increased periodically. There is no limit to the number of people you can give gifts to which qualify for the annual exclusion. To qualify for the annual exclusion, the gift must be one that a recipient has full control over.

### **Asset Based Valuation Approach**

Most assets are reported on the company's books at their acquisition value net of depreciation where applicable. These values must be adjusted to fair market value whenever possible.

### **Asset Sale**

A form of acquisition whereby the seller of a corporation agrees to sell all or certain assets and liabilities of a company to a purchaser. The corporate entity is not transferred.

**Board of Directors**

A body of elected or appointed members who jointly oversee the activities of a company or organization.

**Bond**

An insurance policy used to ensure a legal representative will do his job and not misuse or steal funds he is controlling. The bond guarantees that a certain amount of money will be paid if a party is injured due to acts of the legal representative.

**Book Value**

With respect to assets, the capitalized cost of an asset less accumulated depreciation, depletion or amortization as it appears on the books of account of the enterprise. With respect to a business enterprise, the difference between total assets (net of depreciation, depletion and amortization) and total liabilities of an enterprise as they appear on the balance sheet. It is synonymous with net book value, net worth and shareholder's equity.

**Business Income Coverage**

Insurance covering loss of income suffered by a business when damage to its premises causes a slowdown or suspension of its operations during the time required to repair or replace the damaged property.

**Business Interruption Insurance**

Covers expenses incurred if the business is interrupted by fire or other events, as well as lost profits.

**Business Valuation**

The act or process of arriving at an opinion or determination of the value of a business or enterprise or an interest. This value is utilized by financial participants to determine the price they are willing to pay or receive to consummate a sale of business.

**Capitalization (Exiting the Company)**

The conversion of income into value. The capital structure of a business enterprise. The recognition of expenditure as a capital asset rather than a period expense.

**Capitalization (Asset Protection)**

The total amount of the various securities issues by a corporation. Capitalization may include bonds, debentures, preferred and common stock, long term debt and surplus. Bonds and debentures are usually carried on the books of the issuing company in terms of their par or face value. Preferred and common shares may be carried in terms of par or

stated value. Stated value may be an arbitrary figure decided upon by the board of directors or may represent the amount received by the company from the sale of the securities at the time of issuance.

### **Capitalizing Net Income**

Determining a future value for the company by dividing the pro forma net income by the required Return on Investment (ROI).

### **Cash Value**

The equity amount available to the policy owner when a life insurance policy is surrendered to the company, or the amount upon which the total available for a policy loan is determined. During the early policy years in a traditional whole life policy, the cash value is the reserve less a surrender charge; in the later policy years, the cash surrender value usually equals or closely approximates the reserve value.

### **Charitable Gift Annuity**

An arrangement whereby the donor makes a gift to charity and receives back a guaranteed lifetime (or joint lifetime) income based on the age(s) of the annuitant(s).

### **Charitable Lead Trust**

An arrangement whereby the charity receives an income from a trust for a period of years, then the remainder is paid to non-charitable beneficiaries (generally either the donor or his or her heirs).

### **Charitable Remainder Trust**

A trust used to make donations of property or money to a charity so the person making the gift or donation can obtain a tax advantage. In a charitable remainder trust, the donor reserves the right to use the trust property during his life or some other specified time period, and when the agreed period is over the property goes to the charity.

### **Codicil**

A written change or amendment to a will.

### **Community Property**

Some state laws require that all assets acquired during a marriage belong equally to both spouses, except for gifts and inheritances given specifically to one spouse. The eight states with such laws are known as community property states. The eight states are Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas and Washington. Puerto Rico also uses the community property system, and Wisconsin has a modified community property system.

**Conservator**

A person appointed to be legally responsible for the management of property and money belonging to a minor or incompetent person. The conservator may act as the guardian or the guardian may be a separate person and the conservator will just work with the guardian.

**Conservatorship**

A court controlled program where a conservator is appointed by the court to manage the monetary affairs of a person(s) who is unable to manage his/her own affairs.

**Corporate Owned Life Insurance (COLI)**

Life insurance owned by a corporation, insuring the lives of its employees. COLI is often used to indemnify the corporation for loss of a key employee or as a supplemental benefit for key employees.

**Corporation**

A corporation is a business or organization formed by a group of people, and it has rights and liabilities separate from those of the individuals involved. Two of the most common options of incorporation are:

*C-Corporations* may be a public or privately held company. Usually shares are held by the founders (often a family), by board members and by private investors, such as venture capitalists, who may or may not sit on the board of directors. While public C-Corporations have far more stringent reporting requirements than privately held corporations, both must have annual shareholder meetings and minutes of those meetings must be recorded.

*S-Corporation* is a regular corporation that has between 1 and 100 shareholders and that passes-through net income or losses to shareholders instead of being taxed at the corporate level. Corporations must meet specific eligibility criteria, and they must notify the IRS of their choice to be taxed as an S-Corporation within a certain period of time.

**Custodianship**

An ownership arrangement in which property management rights are given to a custodian for the benefit of a child beneficiary under the Uniform Gifts to Minors Act or the Uniform Transfers to Minors Act; a custodian's duties resemble those of a trustee, although the custodian does not take legal title to the trust property and custodianship ends when the minor reaches the age of majority as specified by state law. May also apply to property management rights of individuals who are determined to be incompetent to handle their own affairs.

**Death Benefit Only Arrangement**

A type of deferred compensation arrangement in which an employer agrees to pay only a death benefit to a deceased employee's heirs rather than the customary retirement benefit (and perhaps ancillary benefits) associated with conventional deferred compensation.

**Defined Benefit Plan**

A qualified plan in which the company specifies the benefit the plan will deliver often driven by a formula of salary, years of service, etc. Typically involves only company contributions; company bears the investment risk. (Examples: pension or cash balance plan).

**Defined Contribution Plan**

A qualified plan in which the company defines the contribution it will make to the employee's account in the plan rather than a fixed benefit the employee will receive. Typically involves both company and employee contributions; employee bears the investment risk.

**Direct Transfer**

The movement of a tax-deferred retirement asset from one plan or custodian directly to another. A direct transfer is not a withdrawal and does not incur any taxes or penalties.

**Directors & Officers Insurance**

Indemnifies officers and directors of the company for expenses incurred as a result of acting on behalf of the company.

**Disclaimer**

The refusal of a beneficiary to accept property willed to him. When a disclaimer is made, the property is generally transferred to the person next in line under the will. A disclaimer is also called a renunciation. A disclaimer must be filed within nine months from the date of death.

**Durable Power of Attorney**

A document established by an individual (the principal) granting another person (the agent) the right and authority to handle the financial and other affairs of the principal. The Durable Power of Attorney survives through the period of incompetence of the principal.

**Durable Power of Attorney for Health Care**

A document established by an individual (the principal) granting another person (the agent) the right and authority to handle matters related to the health care of the principal. The Durable Power of Attorney survives through the period of incompetence of the principal.

**Earn-out Formula**

The portion of the purchase price that is contingent on future performance. It is payable to the sellers only when certain pre-defined levels of sales or income are achieved in the years after acquisition.

**EBITDA**

Earnings before interest, taxes, depreciation, and amortization.

**Employee Benefits Liability**

Liability of an employer for an error or omission in the administration of an employee benefit program, such as failure to advise employees of benefit programs. Coverage of this exposure is usually provided by endorsement to the general liability policy but may also be provided by a fiduciary liability policy.

**Employee Dishonesty Coverage**

Employee dishonesty coverage protects an employer from financial loss due to the fraudulent activities of one or more employees. The coverage includes protection for loss of money, securities, and other property of the insured.

**Employee Stock Ownership Plan**

An Employee Stock Ownership Plan (ESOP) is essentially a stock bonus plan in which employer stock is used for contributions. A "KSOP" plan also includes §401(k) Plan features. Employer contributions are tax deductible and are not currently taxed to the employee. Earnings accumulate income tax deferred and distributions are generally Endorsement Method (Split Dollar)

**Employment Practices Liability Insurance**

Employment Practices Liability Insurance provides protection for an employer against claims made by employees, former employees, or potential employees. It covers discrimination (age, sex, race, disability, etc.), wrongful termination of employment, sexual harassment, and other employment-related allegations. It covers the company, including its Directors and Officers.

**Equity Split-Dollar**

An arrangement in which the employer's share of the cash value and death benefit of life insurance on an employee's life is confined to its aggregate net premium payments; any cash value in excess of the employer's premiums inures to the benefit of the other party (employee or third party).

**ERISA**

The acronym for the Employee Retirement Income Security Act of 1974, a federal law that established minimum standards for certain employee benefit plans, especially qualified employer retirement plans.

**Errors and Omissions Insurance**

Liability insurance policy that provides protection against loss incurred by a client because of some negligent act, error, or omission by the insured.

**Estate Taxes**

Taxes imposed on the "privilege" of transferring property by reason of death. Estate tax is most commonly used in reference to the tax imposed by the Federal Government rather than the state government. Estate taxes are intended to raise revenue for the government and break up a family's wealth, so that the nation's wealth doesn't concentrate in the hands of a few families.

**Executor/ Executrix**

The person (male/female) named in a will to manage a decedent's estate. The more modern term is a "personal representative," which removes any reference to the sex of the person.

**Exemption Equivalent**

When property is given as a gift or passed to heirs as part of an estate, it is subject to federal estate and gift tax laws. Each person is given a tax credit (the "unified credit") that can be used to offset the tax assessed against a specific amount of property. The amount of property that results in a tax exactly equal to the unified credit is known as the "exemption equivalent." Technically, no property is exempt from federal estate and gift taxes, but the term exemption equivalent is commonly used. Stated another way, the unified credit is equal to the amount of tax due on a gift or estate transfer of property that has a value equal to the exemption equivalent amount.

**Fidelity Insurance Coverage**

Fidelity liability insurance covers the company in the event of employee theft.

**Fiduciary**

A person with the legal duty to act primarily for another's benefit in a position of trust, good faith, candor and responsibility. "Fiduciary" is often used as an alternative term for "trustee."

**Fiduciary Bond**

A judicial bond that guarantees that a court-appointed fiduciary, trustee of the plan, an executor or guardian, performs all duties. A fiduciary bond is required by the court in order to protect the person for whom the fiduciary is acting, such as a ward.

**Fiduciary Liability**

The responsibility on trustees, employers, fiduciaries, professional administrators, and the plan itself with respect to errors and omissions in the administration of employee benefit programs as imposed by the Employee Retirement Income Security Act (ERISA).

**Financial Recasting**

Financial recasting of the historical financial statements adds back items such as superfluous, excessive, or discretionary expenses and non-recurring revenues and expenses. Recasting provides an economic view of the company, and allows meaningful comparisons with other investment opportunities.

**Fringe Benefits**

Non-wage compensation provided to employees in addition to their normal wages or salaries.

**General Power of Attorney**

A legal document that, when properly executed, gives one person (the agent) full legal authority to act on behalf of another (the principal). The scope of the document can be as broad or narrow as you desire as defined in the document. A general power of attorney becomes invalid when the principal dies or becomes incompetent.

**Gift Taxes**

Taxes levied by the Federal Government on gifts above the annual exclusion. Gift taxes and estate taxes have been "merged" into a single tax called the "unified tax."

**Goodwill**

The amount by which the consideration paid exceeds the fair market value of the company's operating assets. Goodwill is considered an intangible asset.

**Grantor**

The person who establishes a trust and transfers assets into it. Other terms for the "grantor" include "trustor" and "settlor."

**Grantor Trust**

A trust in which the person establishing the trust retains enough "ownership rights" or "incidents of ownership" that the person is treated by the IRS as the owner of the trust assets for tax purposes. The right to revoke the trust is sufficient to make the trust a grantor trust.

**Group "Carve Out" Life Insurance Plan**

A plan that seeks to cover a limited number of employees, hence 'carved out' of the larger employee group. The plan can therefore be designed to provide higher benefits to key employees.

**Group-Term Life Insurance Program**

An employer may provide employees with life insurance coverage through an IRC §79 group-term policy, the first \$50,000 of which generally produces no taxable cost to the employee.

**Guarantor**

A party who guarantees repayment of a loan, using their own assets if necessary.

**Guardian**

A person designated by court appointment and given the responsibility of managing the personal affairs of a minor child or a person that is legally incompetent to manage his or her own affairs.

**Incapacitated**

A person who is legally incapable of managing his or her own business affairs. A person may be permanently or temporarily incapacitated. A probate court usually decides if a person is incapacitated or not. "Incapacitated" is often used interchangeably with "incompetent."

**Incidents of Ownership**

Any interests or rights that an individual maintains in an asset, including property and insurance, that allow the person to change, modify, use or benefit from that asset.

**Income Valuation Approach**

A general way of determining value of a business, business ownership interest or security using one or more methods wherein a value is determined based on anticipated benefits. Generally, the income approach determines value by calculated the net present value of the benefit stream generated by the business.

**Incompetent**

A person who is legally incapable of managing his or her own business affairs. A person may be permanently or temporarily incompetent. A probate court usually decides if a person is incompetent or not. "Incompetent" is often used interchangeably with "incapacitated."

**Independent Trustee**

A trustee who is unrelated to the person who establishes a trust (the grantor) and the beneficiaries of the trust. Unrelated attorneys, banks, corporations, etc., are usually chosen to act as independent trustees. The IRS requires a trust to have an independent trustee if the trust is to achieve certain estate tax and income tax benefits available to irrevocable trusts (not living trusts).

**Individual Retirement Account (IRA)**

A tax-deferred retirement account for an individual that can be established by a person with earned income. Earnings accumulate tax-deferred until the funds are withdrawn. Prior to age 59½ a 10% penalty will apply, and after 59½ there is no penalty. The minimum distribution must begin at age 70½.

**Intangible Assets**

The intangible assets will usually consist of goodwill and going concern value, certain types of intangible property that generally relate to the workforce, information base, know-how, customers, suppliers, or systems in place producing cash flow, proprietary rights (such as; patents, copyrights, trademarks, or trade names), covenant not to compete or similar items.

**Irrevocable Trust**

A trust that cannot be changed, canceled, or "revoked" once it is set up. A "living trust" is not an example of an irrevocable trust. Insurance trusts and "Children's Trusts," or "2503 Trusts," are examples of irrevocable trusts. Irrevocable trusts are treated by the IRS very differently than revocable trusts.

**Joint Ownership**

The situation where two or more people own the same piece of property together. The property can be "owned" by the people as joint tenants, tenants in common, tenants by the entirety and other legally defined relationships.

**Joint Tenancy**

When two or more people take title to the same property and simultaneously each owns 100% of the property, or has full rights to the property. At the death of one joint tenant, his or her share immediately transfers to the ownership of the survivor(s).

**Keogh Plan (HR-10 Plan)**

Retirement plan individually adopted by self-employed persons.

**Key Man Life Insurance**

Life insurance owned by a business entity on the life of a key individual that will, in the event of his or her death, offset a loss in earnings and provide the funds necessary to find, hire, and develop a replacement.

**Letters of Administration**

Document issued by the probate court giving the administrator authority to administer the estate.

**Letters Testamentary**

A formal court order (document) issued by a probate judge giving the personal representative authority to conduct business, contract, sell estate property, pay bills, distribute estate property, and otherwise act on behalf of the estate.

**Liability Insurance**

Covers liability for injury to person or property caused by the company or its employees. Liability insurance can be purchased in a separate policy and attached to other coverage such as automobile, property or a commercial policy.

**Life Estate**

The right to have all of the benefit from a property during one's lifetime. The person with the right doesn't own the property, and when he or she dies, the property is not included in his or her estate.

**Life Insurance Trust**

A type of irrevocable trust used to hold life insurance. When a life insurance policy is held in an insurance trust, it is protected from estate taxes when the insured dies; provided the trust is established properly, managed properly, and the insured does not retain any "incidents of ownership."

**Limited Liability Company (LLC)**

A limited liability company (LLC) is a legal form of business offering limited liability to its owners. An LLC combines the tax flexibility of a partnership with the personal liability protection of a corporation. An LLC can elect to be treated as a C Corp or S Corp for federal tax purposes. LLC owners report their share of business profit and loss on their personal tax returns, similar to tax reporting for a general partnership. An LLC can elect to be member-

managed or manager-managed. Choosing to operate by member-management creates a flat member or partnership structure. Choosing manager-management creates a two-tiered management structure potentially convertible into a corporation, with the attendant tax consequences.

LLC's use IRS Form 1065 (if taxed as a partnership) and Schedule SE (Self-Employment Tax). LLC's are organized with a document called the "articles of organization," or "the rules of organization" specified publicly by the state; additionally, it is common to have an "operating agreement" privately specified by the members. The operating agreement is a contract among the members of an LLC, and it governs the membership, management, operation and distribution of income of the company.

Managers are the individuals who are responsible for the maintenance, administration and management of the affairs of an LLC. In most states, the managers serve a particular term and report to and serve at the discretion of the members. Specific duties of the managers may be detailed in the articles of organization or the operating agreement of the LLC. In some states, the members of an LLC may also serve as the managers. Owners are referred to as 'Members'. Unless the articles of organization or operating agreement provide otherwise, each governing person or member has an equal vote in the management of the LLC.

### **Limited Liability Partnership (LLP)**

A limited liability partnership, or LLP, is a business organization that allows limited partners to enjoy limited personal liability. It operates much like a limited partnership, but gives each member of the LLP an equal voice in managing the business. It also protects members from personal liability, except to the extent of their investment in the LLP. Generally, partners in a limited liability partnership aren't responsible for another partner's debts, obligations, or liabilities resulting from negligence, malpractice or misconduct.

### **Limited Partnership (LP)**

A business organization with one or more general partners, who manage the business and assume legal debts and obligations, and one or more limited partners, who are liable only to the extent of their investments. Limited partners also enjoy rights to the partnership's cash flow, but are not liable for company obligations.

### **Liquidation Value**

The value of a company assuming the assets of the company are sold piecemeal (not as part of an ongoing business enterprise) with-appropriate time ' for exposure to the marketplace.

**Living Will**

A document defining your "right to die." It usually states that you do not want to have your life artificially prolonged by modern medical technologies. You can specifically define the means which you do not want used or do want used.

**Marital Deduction**

The unlimited deduction allowed under federal estate tax law for all qualifying property passing from the estate of the deceased spouse to the surviving spouse. The value of the property passing to the surviving spouse under the marital deduction is "deducted" from the deceased spouse's estate before federal estate taxes are calculated on the estate. Proper planning and use of the deduction allows more property to pass estate tax free to the family.

**Market Valuation Approach**

A general way of determining a value indication of a business, business ownership or security using one or more methods that compare the subject to similar businesses, business ownership interests or securities that have been sold.

**Non-Operating Assets**

Assets shown on the company's balance sheet that are not used in the operation of the business. That is, "extra" assets that are not necessary to generate the revenue and cash flow stream being valued.

**Nonqualified Deferred Compensation Plan**

A contractual arrangement that calls for paying an individual or group of executive's future benefits. It does not qualify for favorable tax treatment, but has far fewer restrictions than qualified plans. Non-qualified plans are unsecured and subject to risks; they must remain "unfunded" to avoid current taxation.

**Normal Working Capital**

The amount of working capital needed by the company to sustain operations throughout the year. Calculated as the average of current assets (which include a normal amount of necessary cash) minus current liabilities on a monthly basis over the most recent twelve months.

**Per Stirpes**

The most common way of distributing an estate such that if one of the children is dead, his or her children share equally in his or her share.

**Performance Bond**

Written guaranty from a third party guarantor (usually a bank or an insurance company) submitted to a principal (client or customer) by a contractor on winning the bid.

Performance bond ensures payment of a sum (not exceeding a stated maximum) of money in case the contractor fails in the full performance of the contract.

**Perpetuities Savings Clause**

A "safety net" clause included in most trusts, which automatically terminates the trust at the last possible moment to prevent any possible violation of trust law caused because the general terms of the trust did not properly provide for a termination of the trust as required by law. Under most state laws a trust must have a finite "life" and end prior to the time required by law.

**POD Account**

A bank account that is designed to avoid probate. It is a contract between the bank and the account holder guaranteeing that, upon the account holder's death, the bank will pay the balance of the account to whoever is designated to receive the account.

**Pour-Over Will**

A will which contains a clause that transfers some or all of the assets that pass through the will into a trust for final distribution from the trust. The will's assets are said to "pour over" into the trust.

**Power of Appointment**

The power given to a person, by appointment in a will or a trust, to distribute the property that passes through the will or trust at the discretion of the person appointed. Other than to give the appointed person the authority to make the distribution, the will or trust doesn't make distribution of the property.

**Pro Forma Statements**

Hypothetical statements. Financial statements as they would appear if some event, such as increased sales or production, were to occur.

**Probate**

The legal process which facilitates the transfer of a deceased person's property whether they leave a will or don't leave any will. The court establishes the authenticity of the will (if any), appoints a personal representative or administrator, identifies heirs and creditors,

directs payment of debts and taxes, and oversees distributions of the assets according to the will or state law in the absence of a will.

### **Products Liability Insurance**

The liability for bodily injury or property damage incurred by a merchant or manufacturer as a consequence of some defect in the product sold or manufactured.

### **Qualified Plan**

Plans that qualify for favorable tax treatment under the Internal Revenue Code, and are subject to a set of restrictive rules and extensive regulations. In particular, the plan cannot discriminate in favor of the highly compensated and has specific limits on the benefits, contributions, and distributions. Qualified plans are secured by a trust, as opposed to a nonqualified plan.

### **Qualified Stock Option Plan**

A tax favored plan for compensating executives by granting incentive stock options (ISOs) to buy company stock. If the plan meets the requirements of IRC §422, the executive is not taxed at the time of the grant or the time of the exercise of the option. Taxation occurs when the stock purchased under the option is sold by the executive. Corporation granting the option does not ordinarily receive a tax deduction.

### **Qualified Terminable Interest Property (QTIP)**

Property qualifying for the marital deduction at the election of the donor or the decedent's personal representative. The spouse retains a qualified income interest in the property for life, with the income payable at least annually. The corpus ultimately passes to a specified beneficiary, under a special power of appointment given to the spouse

### **Ratio Percentage Test**

A test that a qualified pension plan must meet to receive favorable income tax treatment. The pension plan must benefit a percentage of employees that is at least 70 percent of the highly compensated employees covered by the plan.

### **Rule Against Perpetuities**

A rule of law limiting the duration of a trust. Some trusts can go on in perpetuity (forever), but most types of trusts have a maximum duration or life established by law.

### **Section 457 Plan**

A plan which provides an exclusion from gross income for a certain portion of salary deferred by a participant under the plan of a state or local government, a tax-exempt

organization (excluding churches), or of an independent contractor of such government or organization (e.g., a physician providing independent services to a hospital).

### **Simplified Employee Pension (SEP) IRA**

A retirement program for self-employed people or owners of small companies allowing them to defer taxes on investments intended for retirement

### **Sinking Fund Approach**

A benefit funding technique wherein assets are set aside in order to accumulate the necessary funds to pay future benefit expenses.

### **Sole Proprietorship**

Sole Proprietorship is a type of business entity which legally has no separate existence from its owner. All debts of the business are debts of the owner. It is a "sole" proprietor in the sense that the owner has no partners. A sole proprietorship is not a corporation; it does not pay corporate taxes, but rather the person who organized the business pays personal income taxes on the profits made, making accounting much simpler. A sole proprietor may do business with a trade name other than his or her legal name.

### **Split Dollar Plans**

A method of purchasing life insurance in which the premium payments and policy benefits are divided, usually between an employer and employee. It can be a valuable executive benefit that provides life insurance protection for an executive's survivors at a minimal cost to the employee. Split Dollar Plans have a variety of designs but they generally fall under one of the following categories based on policy ownership.

*Economic Benefit Regime:* the employer is the primary policy owner and the key employee's interest in the policy is typically limited to death benefit coverage. The death protection is an "economic benefit" with a value based on a government term insurance table.

*Loan Regime:* the employee or a selected third party is the primary owner of the policy. The employer's premium advances are considered to be loans to the employee. The policy cash values become collateral for the repayment of the premium loans. Loan interest is either paid by the employee or reported by the employee as imputed income.

### **Step Up Basis**

A decedent's capital gains property that passes to others escaping capital gains tax when sold by the person who inherits the property. Persons inheriting capital gains property receive the property at date-of-death fair market value. In effect, the basis in this property

is deemed to be "stepped up" and does not reflect the decedent's original cost basis for determining applicable capital gains tax on the sale of the property.

### **Stock Bonus Plan**

A method of compensating selected executives by issuing company stock in lieu of or in addition to cash bonus compensation. The executive is taxed on the value of the stock as ordinary income and any increase in value of the stock is owned by the executive. The bonus is deductible by the employer if it is reasonable compensation for services rendered.

### **Successor Trustee**

The trustee who takes over when the initial trustee can no longer function.

### **Supplemental Executive Retirement Plan**

A type of non-qualified deferred compensation plan often used to attract and retain executives. Generally, the promised benefits are paid from the employer's general assets, and no amounts are specifically earmarked for future benefit payments. Usually the employee has no option to receive the funds as current compensation.

### **Survivorship (Second-to-Die) Life Insurance**

This type of coverage insures two people and pays the death benefit at the death of the second insured. The premiums are significantly less than two traditional insurance policies because the policy insures two lives. For older individuals with some health considerations, this may be a viable option for coverage. This type of insurance is utilized in the estate planning market as the death benefit is paid after the last spouse's death. The insurance can also be used to equalize an estate or the pay taxes.

### **Tangible Assets**

Tangible assets that may be included in the sale of a business usually consist of accounts receivable, inventory, leasehold improvements, furniture and fixtures, equipment, land and building.

### **Taxable Estate**

The portion of an estate that is subject to federal estate taxes or state death taxes. Technically, all of an estate is subject to federal estate taxes, but because of the unified credit, only estates with a value over the exemption equivalent amount actually have to pay any estate taxes. Therefore, it is common to refer to an estate with a value over the exemption equivalent amount as a taxable estate and an estate with a value under the exemption equivalent amount as a nontaxable estate.

**Tenants by the Entirety**

A way of owning property which, for almost all practical purposes, is the same as joint tenants. Tenancies by the entirety are creations of state law and are used only between husbands and wives, whereas joint tenancies can be used by anyone, not just by husbands and wives, who want to own property jointly.

**Tenants in Common**

A way of owning property in which two or more owners all "share" ownership of the property. The owners can own various percentages of the whole property, unlike joint tenants which each own an equal share. When one owner dies, his or her share does not "automatically" go to the other owner(s), because tenancies in common do not have a survivorship provision like joint tenancies.

**Testamentary Trust**

A trust which is created upon the death of testator and which is specified in his will.

**Unified Tax Credit**

A federal tax credit that reduces the tax liability for various end-of-life taxable income and assets. Primarily, the unified tax credit may reduce one's estate tax liability or taxes on lifetime gifts on a dollar-for-dollar basis. In certain circumstances, the unified tax credit may be applied to a generation-skipping transfer.

**Universal Life Insurance (Adjustable Life)**

A type of permanent life insurance that allows you, after your initial payment, to pay premiums at any time, in virtually any amount, subject to certain minimums. This policy also permits you to reduce or increase the death benefit more easily than under a traditional whole life policy.

**Unlimited Marital Deduction**

The tax law that allows a person to give an unlimited value of property as a gift, or leave an estate of unlimited value to his or her spouse without a gift or estate tax being assessed.

**Valuation Approach**

A general way of determining value using one or more specific valuation methods. (See Asset Based Approach, Market Approach and Income Approach definitions.)

**Valuation Method**

Within valuation approaches, a specific way to determine value.

**Valuation Multiple**

A factor wherein a value or price serves as the numerator and financial, operating or physical data of the company being valued serve as the denominator.

**Vehicle Insurance**

Covers liability for injuries caused by company vehicles and employee vehicles when used for business purposes.

**Vesting**

The process by which employees accrue non-forfeitable rights over employer contributions that are made to the employee's qualified or nonqualified retirement plan account. An issue in conjunction with employer contributions to an employee stock option plan, or to a retirement plan such as a 401(k), annuity or pension plan. The vesting period is a period of time an employee or other person holding a right to something must wait until they are capable of fully exercising their rights and until those rights may not be taken away.

**Whole Life Insurance (Ordinary Life)**

A common type of permanent life insurance is whole life. With this type of policy, premiums generally remain constant over the life of the policy and must be paid periodically in the amount specified in the policy.

**Will**

A legal document stating the intentions of a deceased person concerning the distribution of his or her property, and management of his or her affairs following his or her death. State law dictates the legality of a will.