Business Succession Planning

It's the Last Thing on Your Mind…and Why it Should Be the First

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Succession Planning Technique #1: Leave the Business to a Child/Children

- If you wish to transfer your business to your children, you can provide for such in your estate plan.

Estate Planning Generally: Why Do You Need an Estate Plan?

- If you don’t create one, the State does it for you (intestate succession laws are the “default estate plan”); this can lead to results you don’t want
- Probate avoidance and estate tax minimization
- Avoid family disputes
- Appoint guardians for minor children

The Basic Estate Plan

- Last Will and Testament
- General Durable Power of Attorney (very broad powers)
- “Statutory Short Form” Power of Attorney (for financial matters)
- Health Care Directive (your wishes on health care matters, especially treatment of terminal conditions)

What About Trusts?

- Use of a revocable trust takes away the need to probate your estate
- BUT: make sure to fund the trust (i.e., re-title your assets in the name of the trust)
- Easy to transfer assets to beneficiaries of a trust upon death of grantor
- Private (probate – public proceeding through a court)
- No tax benefit to a revocable trust

Irrevocable Life Insurance Trusts

- Life insurance proceeds are non-probate assets
- BUT: life insurance proceeds are included in your taxable estate for estate tax purposes
- Solution: irrevocable life insurance trust (ILIT); after the policy/policies have been in the trust for three (3) years, the death benefits will be excluded from your taxable estate

Special Considerations for Business Owners

- Nothing specific in intestacy statutes regarding transfers of businesses
- Failure to create an estate plan or business succession plan can result in adverse consequences to the business
- If you have children involved in the business and others who are not, your estate plan might provide for unequal distribution of other assets to account for transfer of business to less than all children.

Reviewing & Updating Your Estate Plan

- Marriage/Divorce
- Death of a spouse
- Children
- Change in financial circumstances
- Regular review and updating of your plan is a <u>must</u> in order to avoid unintended consequences!

Succession Planning Technique #2: Buy-Sell Agreement

- Often thought of as the “business prenuptial agreement”, the buy-sell agreement can be a succession planning tool.

- Transfers on death funded with cross-policies of life insurance; life insurance proceeds received by surviving owner paid to deceased owner’s estate in exchange for deceased owner’s interest in company.

Succession Planning Technique #3: Sale to Third Party

- Asset sale vs. stock sale
- Preparing your business to sell takes time and requires a "team of advisors":
  - Business Attorney (transaction itself)
  - Estate Planning Attorney (estate plan creation)
  - CPA (financial statements, tax structure of sale)
  - Financial Advisor (investment of sale proceeds in order to maintain selling owner's desired lifestyle)
  - Other advisors as needed (business broker, etc.)

Succession Planning Technique #4: Transfer to Employees (ESOP)

- Employee Stock Ownership Plan ("ESOP")
- In an ESOP, a company sets up a trust fund, into which it contributes new shares of its own stock or cash to buy existing shares.
- Alternatively, the ESOP can borrow money to buy new or existing shares, with the company making cash contributions to the plan to enable it to repay the loan.
- Regardless of how the plan acquires stock, company contributions to the trust are tax-deductible, within certain limits.
- Shares in the trust are allocated to individual employee accounts; over time, employees' shares become vested.
- Owners of privately held companies can use an ESOP to create a ready market for their shares. Under this approach, the company can make tax-deductible cash contributions to the ESOP to buy out an owner's shares, or it can have the ESOP borrow money to buy the shares

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Questions?

Thank You!

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