BUSINESS SUCCESSION PLANNING

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Although owners of privately held companies may feel too busy running their businesses to have time to worry about succession planning, failure to have a business succession plan in place on an owner's death can result in higher estate taxes, uncertainty about the leadership of the business, and even failure of the business.

One of the most important reasons to have a succession plan is to provide for continuing and capable management. If a business has no management bench strength, loss of the owner is likely to result at best in a fire sale with substantial loss of the business's value. Planning for continuing control of the business is therefore essential, even while the owner may be engaging in transactions that remove some of the value of the business from his or her taxable estate. Planning for the inevitable eventual change in management and ownership also has other benefits, including providing initial security for the owner's retirement and disability, providing for dependents, assisting in maintaining family harmony, and reducing taxes.

According to Will Kelly, CFP®, managing director at United Financial Capital Partners, "One of our fundamental business beliefs is that it's always the right time to plan. If you are in the enviable position of having created an enterprise with sustainable value, take advantage of the resources available to ensure that the value endures."

Various methods are available to transfer ownership to family members, co-owners, employees, and others. The best method for each business will depend on the structure of the business, the business owner's goals, and the nature of the transfer. Options include, among many others, an employee stock ownership plan (ESOP) and negotiating an arms-length sale, roll-up transaction, or leveraged recapitalization.

In cases where a business owner wishes to pass the business down to younger family members through gifts or sales, a shareholders' agreement is usually advisable. One purpose of a shareholders' agreement is to prevent stock (or LLC or partnership interests) from being transferred outside the family, as can happen as a result of a child's divorce. Transfer restrictions can also have tax advantages by reducing the value of transferred shares for tax purposes.

Many small businesses are jointly owned by two or three partners, shareholders, or members. There may be no intention to pass ownership down to children. In these instances, a well-designed buy-sell agreement is advisable to provide certainty and continuity on the death of one of the owners. Such agreements are often funded by

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life insurance. Cross-purchase life insurance plans can provide liquidity to the estate of a deceased partner with estate tax advantages.

Because income, gift, and estate tax exposure varies in each individual situation depending on the ownership and transfer method, a good business succession plan takes into consideration the owner's estate plan and helps minimize tax consequences. Additional estate planning can be accomplished through the use of trusts.

Mr. Kelly notes, "One of the issues we emphasize is the importance of having coordination among the various advisors. They often include attorneys, accountants, financial advisors, and insurance specialists."

It takes time to select the right succession plan, to find the right people to implement it, and to execute the plan. The right time to plan is when everyone involved is healthy and actively involved in the business.