

FINANCE QUARTERLY

Two Plans You Need to Get Right

By Kent Tsukamoto, Accuity LLP

“When did this happen?” “It was all so sudden!” “How is the family coping with their loss?” “What about the business?” “Are the employees OK?”

Sound familiar? In the 30 years that I have practiced as a Certified Public Accountant, few situations have been more traumatic or heart-wrenching than dealing with

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the surviving family members of business owners who failed to consider or implement two basic plans. These plans - the family’s overall Estate Plan and the Business Succession Plan -- are critical to the continuity and the survival of family-owned businesses. In closely-held businesses especially, these two plans intersect, converge and should complement each other. While these plan concepts are simple, their execution, however, can be psychologically difficult.

The Estate Plan

Reluctance or procrastination about addressing this critical area all points back to our feelings about our mortality. Almost no one wants to think about their inevitable death, so planning gets deferred and relegated to a back burner. Busy creating value for their businesses by providing and marketing goods and services, many business owners are also too preoccupied to worry about and deal with an Estate Plan. Wise ones, however, have the vision and foresight to plan for various outcomes. In a way, the Estate Plan is a business owner’s ultimate “Plan B.” And the process is actually very simple.

I normally ask two questions when working with a business owner on an Estate Plan. The first one is, “Ignoring any tax matters, when you are gone, where do you want your assets to go and when?” The answers often reveal many insights about how the owner thinks and feels about family members and potential recipients.

The second question is “Who do you want to be on your planning team?” Typically, I want to work with an estate planning lawyer, a banker, an investment advisor and an insurance consultant. This team should work well together in a coordinated effort to carry out the client’s wishes. We then design and



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recommend various strategies to minimize, defer or eliminate transfer taxes.

Be aware that if no planning is implemented, state law and the federal government will determine who gets what and when, taking the decision-making out of the leader's and family members' hands. The U.S. government imposes taxes upon a donor for transfers made during life (gift tax) and upon death (estate tax). The top marginal tax rate is currently a hefty 45 percent. While a detailed discussion about the tax system is beyond the scope of this article, the one concept that should be emphasized is that every person has an estate tax "exemption" (currently \$2 million) that should be utilized in a properly executed plan. In a sizeable estate, the prudent use of trusts and life insurance policies can make a significant difference in desired outcomes and the preservation and transfer of wealth to the next generation.

The Business Succession Plan

"As a business owner, my most important job is finding my replacement." This should be the leader's mantra if a business is to succeed and flourish beyond one generation. Grooming the next generation of leaders can be particularly challenging and sometimes difficult in a family

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business setting. Founders are often hard-working, charismatic and strong-willed individuals. Their children may share these traits, but even they may need time away from the family business to develop their own views, perspectives and skills. This is a rule that many family businesses implement – you must work elsewhere and be promoted twice before you can work in the family firm.

In our practice, we are fortunate to work with a number of family-owned companies that have successfully transitioned into the third or fourth generation of leaders. A common observation of these companies is that they emphasize constant communication, mutual respect and an understanding of when to wear your business hat and when to wear your family hat.

An effective succession plan requires that the leader/patriarch/matriarch shares and communicates a vision of the values that are most important to the Family and likewise, the Company. Ideally, the business is run as a



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meritocracy and those family members who are most capable eventually assume a leadership role. This is then communicated to the rest of the family and the founder's estate plan typically will integrate ownership and control to the expected leader. If no family member rises to or desires the leadership role, then outside professionals or other exit strategies can be considered.

The major step in establishing a succession plan is to recognize the need for one. Then the leader should share his/her thoughts with the entire family to provide clarity to members. Suddenly losing your leader is traumatic. Intra-family litigation, because there was no clear road map or successor named by the founder, is truly tragic for both family and business.

For family-run businesses, an Estate Plan and a Business Succession Plan are two important decisions that you want to get right and to revisit regularly to ensure they are still relevant and consistent.

In the final analysis, the greatest legacy a business owner can leave to the community is a thriving, vibrant and successful business that will last. The greatest legacy the owner can leave the family is strong values and wonderful memories.