

How to Get 'Success' Out of Succession Planning

by Tom Sigmund, Esq.

Business succession planning is inherently complex. It requires a comprehensive, dynamic and integrated system of business solutions, ranging from management succession and executive compensation to mergers and acquisitions, ownership transfers, tax reduction, and financial and estate planning. Planning requires custom-designing each of these solutions to meet the goals and objectives of the business and its owner(s).

When a business is family owned, succession planning is even more complex — a combination of retirement planning, estate planning and business continuity

planning. "People issues" often are at the forefront, and need to be managed with care. Succession planning for family owned businesses should have three main objectives: to pass control of the business to those worthy and active in the business; to provide for the financial well-being of the current business owner(s) and his or her (their) loved ones; and to treat inactive family members fairly.

Start Planning and Implementation Early

Family business succession planning should be a long-term process. Usually, the owners of family businesses will find incremental changes to the way they do business more effective

than implementing an all-encompassing plan. All-encompassing plans often lack necessary input from family members, and don't benefit from the trial-and-error of an extended process.

A good starting point is to determine the value of the business. Obtaining a valuation from a professional valuation firm will provide critical information for life insurance planning, gifting, and strategic ownership of the business. It will also provide information for addressing transfer taxes that may be associated with gifts and the death of the founder/owner. (See sidebar next page.)

Starting the planning process early is imperative. Delays can have negative results, such as making saving for retirement difficult



or impossible. Insurability and other issues may arise. If planning is hurried, there may not be enough time to work out conflicts or to take advantage of many tax savings vehicles. For family members to have an ongoing dialogue, they'll need ample time too.

Communicate and Build Consensus

Poor communication and consensus-building skills can easily create distrust and greatly decrease the odds of perpetuating the family business. Furthermore, while some family businesses emphasize business values over family, other family businesses are first a family and second a business. If treated the same way in succession planning, the results can be disastrous for the business.

In a family business context, the approach to conflict resolution shouldn't necessarily be the same as in the non-family business context. Gravitating to a single dispute resolution procedure may not be appropriate in the family business context. Requiring that the business owner, the family, and other key personnel actually meet to discuss issues with the assistance of family counsel or the company's board of directors is a better process than seeking relief through mediation or arbitration, which should be the last resort. A meeting is preferable to taking actions in writing without a meeting.

Provide for Retirement

Family business plans frequently are prepared by one advisor who may not have all of the skills necessary to implement a successful succession plan. For example, if an advisor with estate tax expertise prepares the family business plan, it is likely to have as its primary objective the minimization of estate and

Common Strategies/Tools in Family Business Succession Planning

Estate and business succession planning go hand-in-hand. Planning requires examining strategies such as:

1. Gifting.
2. Life insurance planning.
3. Equitable treatment of active vs. non-active family members.
4. Liquidity.
5. Wealth preservation.
6. Wealth transfers.
7. Trust planning.
8. Retirement planning.

Implementing the succession plan in a manner that effectively addresses tax issues requires tools such as:

1. Long-term rental arrangements.
2. Life insurance trusts.
3. Buy-sell agreements.
4. Split dollar life insurance plans.
5. Grantor retained annuity trusts.
6. Sales to defective trusts.
7. Family limited partnerships.
8. Charitable remainder trusts.
9. Employee stock ownership plans.

Succession Planning Terms

Retirement planning relates to the financial and personal needs of the current owner(s).

Estate planning relates to the preservation, protection and distribution of assets.

Business continuity focuses on the future needs of the business.

gift taxes by transferring assets, including the family business, to members of junior generations. Such a plan may pay little or no attention to the senior family members' retirement plans or to other needs.

Family business succession planning requires a multi-disciplined team of advisors. Although minimizing estate and gift taxes is important, the plan must also address the retirement of senior family members. Senior family members should have sufficient assets to retire without the continued support of the family business, allowing them to "retire" in the real sense of the word. If the senior family members' retirement and financial security are too closely tied to the business and their successors, they may not be able to ignore the business and entrust it to junior generations.

Choose Criteria for a Successor

For the succession plan to succeed, the family must agree on the criteria for selecting the successor(s). Only then should family members focus on who, if anyone, best fits the criteria. In some family business situations, there may be no appropriate successor. In such situations, it may be more appropriate to sell the business rather than for it to remain in the family. For some, "selling" the business to employees through an employee stock ownership plan might be the best solution.

Conclusion

A succession plan won't succeed unless the business owners and their family have the desire, interest and commitment to move forward. Only once that commitment is made should the process begin — but the sooner, the better. ■

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