OLD NORTH STATE TRUST, LLC

Succession Planning Helps Pass Business to Next Generation

For successful business owners, a vital part of the estate planning process is to think about what will happen to their business after their deaths. Succession planning can be a serious challenge for someone whose entrepreneurial vision and drive created a thriving enterprise.

It is a challenge because so many businesses are so closely associated with their founders. Their success is a good thing because it has let them build significant assets for themselves and for their families. That success can be bad, however, if the owners don't have a clear idea of who should take control of the business after they are gone. Even if they can answer the "who" question, they still have to figure out the "how."

Finding the best answers to both questions is the essence of what succession planning is all about. One of our specialties as trust experts is to help with the planning, and then to help with the execution when the time comes to transfer the business.

This is not solely an issue for owners of corporations, or even of retail businesses and similar "storefront" operations. Many professionals and sole proprietors have to face succession issues, as well. For example, some of our clients are doctors in solo practices. However the enterprise is structured, careful succession planning can preserve assets, minimize taxes, and put the business's day-to-day management in the most capable hands.

One helpful tool can be life insurance. A carefully chosen life insurance policy can provide cash needed to replace the deceased business owner's expertise, or to meet other immediate needs. We often include insurance policies in our clients' succession plans. What is most important, however, is that there is a plan. Each plan should be tailored to each business's particular details, as well as to the owner's family situation and personal wishes.

A useful example is a former client of ours, who has since passed away. He was a physician who had a very successful practice and accumulated a great deal of wealth. Being community minded, he created a foundation to help put some of his wealth to work for causes in which he believed. At the same time, he created trusts for his children, to help them after his death.

He had one other vital concern, which was that his ailing wife's needs would be met, both before and after his own death.

In this case, the succession plan was not intended to keep the business going. As a solo practitioner, he did not have partners to carry on after him. Instead, both his personal and business assets were passed on in a form that his heirs could use to build their own businesses, or meet other personal priorities.

We worked carefully with this client to structure a plan that allocated his assets to his widow, to his foundation, and to his children, exactly as he intended. By taking advantage of tax laws, we ensured that no estate taxes would be paid at his death. Then, afterward, we are continuing to work with the doctor's successors, his foundation and his children, to manage and safeguard his legacy.

This is a win-win scenario all around. It offered the doctor peace of mind, knowing that his wishes would be carried out. It provided for his family, with their individual needs considered. Finally, it continued the doctor's desire to make a continuing contribution to the community that had supported him and his practice.

A thoughtful succession plan is important regardless of whether the client wants to continue the business, or to liquidate it and transfer the assets. In both cases expert advice on taxation and estate administration is essential.

We have seen a sobering statistic that sheds light on why succession planning is so crucial. Even though nine out of ten small businesses in this country are family owned, less than a third of them continue under the second generation. A mere 15 percent make it to the third generation.

Failing to plan ahead for succession can be fatal for a family business. When relatives are involved, decisions are seldom made on a strictly business basis. All the emotions surrounding family relationships, plus the stresses surrounding loved ones' aging and death, can lead to disagreements among heirs and rash decisions that may not honor the founder's intentions.

Among the crucial choices we advise clients to make is deciding who will succeed them in owning and managing the business. Ownership and management don't necessarily go together, by the way. Sometimes the best plan is to put an experienced non-family employee in charge of management, but with the founder's family members continuing as owners. In these arrangements, "The devil is in the details," which is why professional advice is so important.

Another vital decision is to determine the succeeding enterprise's financial structure. A business that started as a sole proprietorship might be passed on, for example, as a family limited partnership, or with some other corporate structure. In all cases, the surviving entity should be structured to minimize tax burdens and clarify decision-making responsibilities.

If we could boil the advice on this subject down to one suggestion, it is to start early. A business owner should begin the estate-planning process, including succession planning, well before the plan is expected to be needed. That allows time to think about priorities, weigh options, and when appropriate to discuss the plans with family members and/or employees.