10 Steps to Plan Your Business Legacy

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The 10 steps you should take right now to preserve and transition family wealth created by your business.

Don't delay focusing on framing the legacy you want to leave for your family and your business. Instead, view legacy planning as an ongoing process that could become critically important at any time. Having a well-designed plan will exponentially increase the likelihood of achieving your goals. Remember: only one in four businesses survives to the second generation, and only one in ten businesses are successfully transitioned to the third.

Step One

Establish goals and objectives: create a legacy plan.

- Your plan doesn't need to be perfect; it may change over time. What's most important is to get a plan in place.
- You may need to have a longer term plan (such as transitioning your business to one or more of your children or readying your company for sale at top value) and a contingency plan to bridge the gap between an untimely death or disability and your ultimate succession goal.
- Consider the difference between ownership and management. You may want your family to continue to own the business, but outside management may be essential if the business is to succeed.

Step Two

Incorporate a business continuity plan.

- Your business is vulnerable if you are suddenly incapacitated or die. Death or disability should trigger a plan that addresses who has the power to vote the stock and details interim or successor executive leadership.
- A gradual transfer of responsibilities to a successor is optimal. If your successor is a family member, make sure they receive the training and education they need to succeed. If your successor is an employee, make sure you properly

incentivize that employee and other key management to stay with your business through deferred compensation plans, stock options or phantom stock and employment agreements.

- If you don't have detailed powers of attorney naming an agent to act for you in the case of a long-term or short term disability, you should. Consider whether the agent you name for non-business decisions is appropriate to be your agent for business matters.
- Consider the important role that a Board or advisory Board can play in the event of a disability or sudden death.

Step Three

Determine your personal needs for cash flow and access to capital.

- Create liquidity outside your business and diversify your wealth.
- Consider having your business appraised to ensure that you are not over or under estimating its value.
- Separate business real estate from the operating company to add flexibility for retention of cash flow from the real estate, or value for children who you determine should not own interests in the operating company.
- Consider deferred compensation arrangements to provide cash flow after retirement and transfer of business interests to the next generation.

Step Four

Execute an estate plan which implements your wealth distribution wishes.

- Consider how your personal and business wealth should be distributed. This plan can and should be reviewed and changed over time.
- Important decisions include:
    - Determining beneficiaries and the limitations/protections to be provided.
    - Identification of Fiduciaries (Trustees/Personal Representatives/Agents/Directed Parties/Trust Protectors).

- Consider how to equitably treat active and inactive children in the business.
- A funded buy-sell agreement can provide a ready buyer for a family that does not wish to continue to have its wealth deployed in the business.
- Consider liquidity needs.

Step Five

Consider how estate taxes may disrupt your wishes.

- Each spouse currently has an exemption of $11.18 million ($10 million subject to annual inflation adjustment). Over and above the exemption, the rate is a flat 40%.
- The "extra" $5 million of exemption each taxpayer received through the 2017 Tax Act is temporary, it expires December 31, 2025.
- Is repeal likely? Probably not as President Trump and the Republican-controlled congress failed to get repeal passed under the 2017 Tax Act.

Step Six

Plan for the possible impact of estate taxes.

- Look to insurance as a short or long term solution.
- Be aware of statutory requirements that trigger the ability to use IRC section 6166 to pay estate tax over installments, and IRC section 303 which provide for tax-free redemptions for estate tax payments.
- Opt to separate high growth lines of the business into separate structures with ownership in the next generation to avoid compounding estate tax issues.
- Consider annual exclusion and medical/educational transfers without use of exemption.

Step Seven

Explore the possibility of large, irrevocable transfers.

- If you are willing to transfer value but not control, consider separating value from control through a stock recapitalization agreement.
- Consider shareholder agreements to protect the business from transfers to outsiders.
- Understand the power of valuation discounts for lack of control/minority interest and lack of marketability.
- Understand the power of leverage and current low interest rates and recognize that rates are rising.
- Consider estate "freeze" techniques such as installment sales to intentionally defective grantor trusts ("IDGTS") and grantor retained annuity trusts ("GRATS") which can freeze the value of your taxable estate while providing cash flow after the business interests are transferred.
- Take advantage of the fact that valuation discounts for minority interests and marketability remain valid. The Obama administration focus on modifying the law through changes in the relevant treasury regulations has been derailed.
- Understand how your charitable objectives can assist in cutting your estate tax burden.

Step Eight

Use irrevocable structures (LLCs/FLPs/Trusts) to hold wealth.

- These structures can be both irrevocable, which will allow you to move growth outside your taxable estate and the reach of your creditors, and flexible, so that if circumstances change, there is access to the transferred assets. Consider the use of:
    - Trustees and Directed Parties.
    - Voting Trusts.
    - Trust Protectors.
    - Grantor trust planning, including incorporating the flexibility to "turn off" grantor trust treatment.

- Multi-generational planning through application of the generation skipping transfer ("GST") tax exemption—give your business the best chance of continuing past your children's generation.
- Spousal Access Trusts that can provide continued access to trust assets and exclusion from the estate for tax purposes and protection from creditors.

- Consider "two-track" planning that functions differently depending on whether or not an estate tax exists at the time of you death.
- For existing structures, consider modification, decanting and other tools available under Wisconsin's new Trust Code.

Step Nine

Build in protection for your legacy.

- Use detailed provisions in your trust documents to protect from:
  - Estate taxes otherwise applied at each transfer.
  - Your beneficiary's creditors.
  - Ramifications of divorce.
  - Costly will and trust disputes and other litigation.
  - Issues with drugs/alcohol/too much wealth.

Step Ten

Review and Refine your plan routinely.

- Changes in tax and other laws, the profitability of your business, your management team and in family dynamics can throw a wrench into a well-crafted plan.

A full text version of legacy planning starts now is also available in a PDF / print friendly version for your convenience

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