

BUSINESS SUCCESSION PLANNING

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Have you started to think about what will happen to your business when you decide to retire? How will you exit your business, seamlessly, and have the money to retire with? For many of us, the business that we have created may be our most significant asset. How to move it from one generation to the other without disruption to our client base requires significant forethought and long-term planning.

Each business situation is unique. There may be family members that wish to continue the operations of the business; there may be valued employees who have worked to build your business with you. Then again, there may be no one. How to create a succession plan from one generation to the other will also be unique to your business, depending upon your specific circumstances. This article merely discusses a few possibilities to think about.

Outright Sale. You can sell your business. Many business owners do this with excellent results, especially those with no family or key employees that wish to continue operating the business. There is still planning that needs to be accomplished prior to the sale, however. You need to establish what your business is worth and determine how you might create more value in your business. Then, you may need time to implement those changes prior to placing it on the market. Finally, you need time to make the transition over to the new owners so your customers remain satisfied. There are problems with an outright sale, the primary one being finding the right buyer. You have spent a considerable amount of your time and effort building the business to where it is today. Much like nurturing a child, you want that business to continue to be successful. If part of your retirement income is attached to its future success, it becomes that much more important that you take the time needed to find the right buyer for your business. Another problem may be financing. Make sure you only risk what you are willing to lose. Finally, there will be tax issues upon the sale. Seek tax advice prior to the sale of your business to ensure favorable tax treatment.

Gifted Interests. Another succession planning tool is to gift interests from one generation to the other. You can do this several ways. Currently, each of us may gift up to \$13,000 a year to any person. If you are married and your spouse will consent, you may gift up to \$26,000 a year without paying any gift tax or without these gifts going against your unified credit. With proper planning, over time you can gift all or a portion of your business with minimal tax consequences. Planning is the key to a gifting program. A business valuation is appropriate every time you make a gift. As you are gifting minority interests, there may also be discounting available to you – in other words, you may be able to gift a larger interest in the business than you think with the proper planning.

Bonus. This is a way to move a percentage interest of the company via a bonus when the future owner clears certain incentives. The bonus results in taxable income for the future owner at the time of the bonus and is subject to withholding and employment tax.

However, the business will receive a corresponding deduction for the bonus. The future owner will have basis in the interest equal to what he paid.

Options. With options, the future owner would receive an option to purchase a percentage interest of the business, exercisable at a future point in time. No tax is due upon grant of the option. However, when the option is exercised, there is tax owed that is calculated on the difference between the value of the interest when the option is exercised and what the future owner pays for the stock. Planning the granting of the options and when they become exercisable is necessary to avoid significant tax issues.

There are also a variety of other vehicles to utilize that will have different tax consequences and could be better for your situation. These vehicles include, but are not limited to, stock appreciation rights, employee stock option plans and phantom stock. Although you may want to utilize only one of the above mentioned vehicles to take your business from one generation to the next, you can use a combination of vehicles as well.

As you can tell from this overview, business succession planning is usually a complicated process, especially when you are designing an exit strategy to meet your future needs without the advantage of a crystal ball. Make sure to give yourself the opportunity of planning time. It is best if you consult your advisors early in the process to help you determine a strategy best fitting your circumstances.