Business Transition Planning: It's Personal

By Daniel Stolfa

Business owners generally have only one shot at getting transition planning right. But most are so focused on the business itself that they risk securing a legacy and preserving wealth by not focusing enough attention on the transition process.

Editor's note: This is the first in an *Independent Thinking* series on business transition planning. This article focuses on personal considerations in selling a business; future articles will look at preparing a business (including a family business) for sale, and options for structuring the transaction.

Almost half of the business owners surveyed by the Exit Planning Institute, or EPI, have not prepared for transition; 79% have no written business plan; and 94% have no written personal plan. That's despite 99% of respondents agreeing that a transition strategy is "important both for my future and the future of the business."[1] The organization estimates that only 20% to 30% of companies will survive a successful transition.[2]

For many owners, the clock is ticking. Of the approximately six million privately held companies operating in the United States, about 63% are owned by Baby Boomers, according to the U.S. Census Bureau.[3] Although it appears that they are holding on to their businesses longer than previous generations (see Jeff Maurer's article on retirement on page 21), it's worth noting that all Boomers will reach the age of 70 or older within the next 15 years. It seems likely that we will soon see a corresponding wave of business transitions, in one form or another.

What form will those transitions take? Failure to plan opens the door to unexpected and even unwanted developments, particularly if a business owner is exposed to divorce, disability, disagreement, death and disaster. Divorce can be crippling to businesses smaller than Amazon when ownership is split. Disability, which can take many forms and is far more likely than an early death, may not directly affect ownership of the business but can most certainly affect profitability if the owner is a key employee. Disagreement is by far the most common exposure and arises anytime two or more owners of a business dispute major decisions. Death and disaster are less common, but can be severe blows to an unprepared business. Good transition planning needs to account for unforeseen pitfalls and to chart a path of the owner's choosing.

So where to start? Many business owners begin by trying to imagine what will happen to the business – their life's work – when the focus should be on their own future. Others expect to fully liquidate their ownership and walk away, assuming the buyer is on board with that plan too. This may not always be the best plan and may leave value on the table. Many want to stay involved in the business, but take some money out and diversify their risk exposure. This is possible, but can affect

[1] Exit Planning Institute, A Local Market Study: The State of Owner Readiness, Twin Cities Metro Area 2017.
[2] IBID.
[3] Colby, Sandra L. and Jennifer M. Ortman. The Baby Boom Cohort in the United States: 2012 to 2060. Current Population Reports, P25-1141. U.S. Census Bureau, Washington, DC. 2014.

business operation and profitability. There are many different ways to achieve these and other transition goals, but they have to be articulated first.

At the personal level, proper transition planning starts with the owner's lifestyle needs and goals. It covers income replacement, expense restructuring, funding the next venture if that's in the cards, and securing the family's future. Thoughtful advance planning should always take full advantage of available tax and legal structures, and for some business owners that may raise the possibility of changing domicile. It is important to proceed carefully and well in advance of a transaction.

Here is a brief outline of the basic components:

GOAL IDENTIFICATION AND DEVELOPMENT

Conduct a comprehensive family wealth and business assessment to prioritize objectives and develop a goals-based wealth management plan.

COMPREHENSIVE INCOME TAX PLANNING

- Minimize income tax liability on the sale of publicly traded or privately held business interests.
- Factor in domicile, residency and trust situs considerations.
- Incorporate income tax planning considerations while developing an overall asset diversification and reinvestment plan.

ESTATE AND WEALTH TRANSFER PLANNING

- Integrate current estate planning "with the corporate succession plan to ensure that all proper documents (e.g., buy-sell provisions, shareholder agreements) are reflective of current goals.
- Implement tax-efficient wealth transfer strategies to transition assets with potential for growth to future generations.
- Current gift and estate tax laws make intergenerational transfers more favorable than in the past.
- Take advantage of lack of marketability and minority interest discounts with closely held private assets.
- Incorporate charitable trusts and entities to facilitate philanthropic objectives while minimizing overall income and estate taxes.

PHILANTHROPIC ADVISORY

Develop a long-term plan to manage and administer charitable-giving vehicles in support of the family's philanthropic mission.

INVESTMENT MANAGEMENT

- Review liquidity needs, risk tolerance and asset allocation.
- Implement investment policy and asset allocation goals for all entities.
- Manage customized investment portfolios in a tax-efficient manner, utilizing both public and private investments.
- Consider asset location with respect to investment strategies across entities.
- Develop post-transaction equity diversification strategies while being mindful of securities laws as they relate to restrictions on selling, hedging and borrowing of restricted stock.
- Utilize tax-efficient concentrated stock management.

Transitioning out of a business, whether through gift, sale or many other techniques, and the start of the next stage of life is a big undertaking – and the considerations are as unique as the people involved. Anyone thinking about a transaction in the next five to 10 years should consult their Wealth & Fiduciary Advisor and other trusted professionals.

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