



Harmonizing Closely-Held Business Succession and Personal Planning: Or... Learn to Stop Worrying and Love the Bomb

If you recognize that parenthetical tagline, you are likely part of the baby boomer generation, like me, and already familiar with worrying about things we have no control over and may have no simple or realistic solutions.

Owners of closely-held businesses are often familiar with this feeling of worry about control, and those who have indulged in HBO's "Succession" understand the concerns that keep us up at night. Succession planning is something many business owners keep at the top of their minds, ranking on their to-do list just above funeral planning and right below tax planning.

However, amidst these concerns lies a crucial realization: succession planning is not just a business strategy but a pivotal component of personal estate planning for business owners. Overlooking the integration of a business succession plan into the broader framework of the business owner's personal estate plan is a missed opportunity. A seamless alignment between these aspects enhances the effectiveness of your overall planning, setting the stage for a more robust and positive future for you and your business.

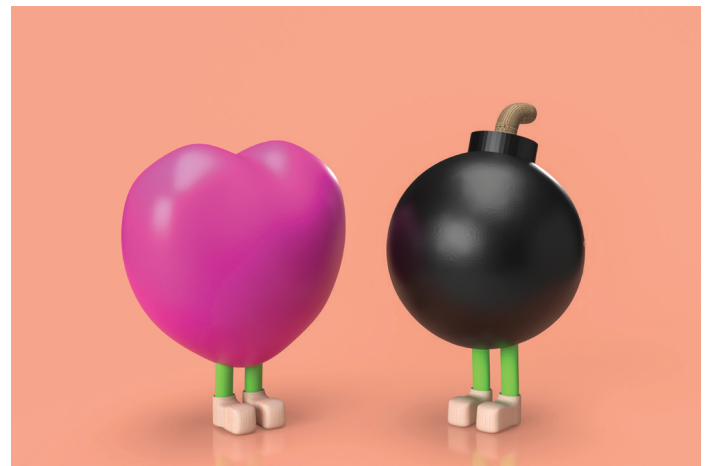
Succession Planning for a "Sole Owner"

More often than not, if the business owner is the sole proprietor, management succession decisions are frequently postponed until well after the business has proven successful—especially in the case of a fledgling enterprise.

Waiting to make succession decisions can be wise for the business owner with a family, especially those anticipating a generational transfer to young children (or relatives). During their formative years, it can be challenging to know which, or if any, of

their heirs are suitable or willing to accept the responsibility of ownership and management of the business. This is even true for companies in the second or later generation of owners.

Considering the complexities surrounding succession planning, here are some of our thoughts for the sole business owner considering legacy planning:



Discuss; Don't Assume.

It doesn't matter who you are; every business owner can fall into this trap. Even as attorneys in private practice, we can assume our children want to follow in our professional footsteps, but assumptions can lead to surprises. We've all heard some version of this story before: "My son clerked for me and then worked in the court system for two summers and then announced that he 'didn't like lawyers' ... imagine that!"

As you know, managing a specialized business or practice is complex and isn't suitable for everyone. Instead of assuming your spouse or child wants to manage the business after you're gone, have a conversation, addressing not only their interest but also the nuances of control and voting rights.

Equity Over Equality.

For those owners who want to be "fair" with the children (this is almost always the case), distributing ownership and control equally may not always be the fairest option for each child's qualifications or interests. Creating voting and non-voting stock classes or providing alternative financial arrangements can help achieve an equitable outcome.

Consider a Transfer of Ownership During Life.

Usually, your successor will have started working for the business well before the transfer of ownership occurs, allowing owners to observe how their heir functions in the business. Transfer of ownership can be done partially or entirely during an owner's life. This process is akin to learning to drive: starting with lessons, gaining a temporary permit, hours of practice, and then the license. Even with licensure, driving is usually monitored under the watchful eye of a parent or two.

Put it in Writing.

Formalizing partial or complete ownership transfer during the owner's lifetime is crucial and often overlooked. Business owners that develop well-crafted agreements and provisions in their Will or Trust can provide clarity and flexibility, allowing adjustments to the plan before the owner's death or incapacity – giving business owners ultimate control and peace of mind.

Transitioning the "Multi-Owner" Closely-Held Business

Unlike the sole proprietorship, ownership of an interest in a small business with multiple owners requires a similar analysis but different tools to harmonize your business succession goals and personal planning:

Discussion is Required.

Like any relationship, communication is key among multiple owners from the start. This involves addressing the significance of asset division in scenarios like business termination, ownership transfer, or an owner's death. Similar to a divorce or handling matters related to death, discussions on management and voting control, capital contribution, and tax consequences are vital during business formation. This typically involves establishing and implementing a Code of Regulations, Operating Agreement, or Partnership Agreement, serving a function similar to a prenuptial agreement.


Create an Equitable Foundation.

In our firm's experience, owners discuss management, control, capital contributions, and division of profit before establishing the business entity. Transition planning for an owner's death or the lifetime transfer of ownership interest is also addressed during business formation. This often involves setting restrictions on voluntary and involuntary lifetime transfers and permitted transfers upon an owner's death.

While we cannot predict the determination of "fairness" without a clear agreement, we know it can potentially lead to disputes and, in some cases, litigation. Owners lacking these agreements may create uncertainties that could escalate into legal issues. To mitigate such risks, establish comprehensive agreements and address these crucial aspects during formation to promote transparency and prevent potential disputes.

Don't Wait to Transfer.

Bestowing ownership while the owner is alive can make leadership transitions smoother. This process works best before the owner's death, following an



agreement with the remaining business owners. Payment, either in cash or installments, should be included in the deceased owner's estate plan.

Make it Official.

For all the reasons noted above, getting your agreements in writing, formalizing relationships in a written document, or registering as a recognized business entity with the appropriate state agency (e.g., the Secretary of State in Ohio) is crucial. Failure to do so may expose the business owners to personal liability to business creditors.

If you really do love "the bomb," you'll be thrilled with the thought of the chaos that follows your death for your failure to provide for a succession plan for your privately-held business interest. The best plan is to let us help you defuse that "bomb" before then. Give your attorney or any member of our Family Wealth and Estate Planning group a call!