LEGACY ADVISORS GROUP

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THE 7 STEPS OF SUCCESSION PLANNING IN 8 INSTALLMENTS

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Introduction

What is the most severe threat to the existence of your business? Some may answer "my competition", or "income and estate taxes". Even others would answer, "rising costs". While these are good answers and are concerns in day to day business operations, there is one issue that overrides everything else regarding threats to your business. The number one threat to your continued going-concern is quite simply the lack of a business succession plan.

The fact of the matter is that, as humans, our existence is finite. Companies, on the other hand, do not suffer the same consequence of being an organic being. Their existence is potentially infinite. While competition, taxes, and increased costs can weigh on a business, the most severe detriment to a business is the loss of an owner or key employee. With a business succession plan, a loss of a key person will trigger specific actions so that the business can continue its operations.

The Problem

Recent research reveals some startling truths:

- Most closely-held businesses are owned by one shareholder.
- A majority of businesses do not have a full and active succession plan in place.
- Fewer than half have a successor in line and prepared.
- More than half of business owners in the United States are 55 years of age or older.
- A good percentage of the owners are 65 years of age or older.

What does this say about the condition of private American businesses? What does this say about the position of business families? Without succession planning, it is a near certainty a great portion of the business value will be lost if the "leader" passes away without a business succession plan. Thousands or millions of dollars which could have been reinvested, saved, or enjoyed otherwise are lost in an instant. Furthermore, failure to implement a business succession plan can result in unnecessary estate taxes.

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A CASE STUDY

A married couple was not allowed to deduct travel expenses for the husband's travel to work at construction sites. In the case, the couple lived primarily in a camper and mostly worked at construction sites in states other than where their primary residence was. The Tax Court held that the couple was not allowed to deduct the travel expenses because neither of them were employed in the state where their primary residence was and they spent little or no time there, meaning they were not "away from home." The expenses were not considered ordinary or necessary because their transient lifestyle was a choice.

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Cover Story

The Solution

It is critical to understand that business succession planning will take time to implement. It is not a day long or hour long process consisting of writing a will or settled with a handshake. A number of steps must be completed in order to receive the maximum value for a business and make the transition as smooth as possible. Also, there are many factors to consider when creating a business succession plan. The age and health of the owner, the industry, the economy, children's interests and ages are just a few factors that must be considered.

The procedures include knowing what business succession is, examining who the potential heirs or buyers are, valuing the company, creating the ideal scenario in which to transfer the business, creating the appropriate legal documents, developing a strategy to deal with estate taxes and establishing a retirement program.

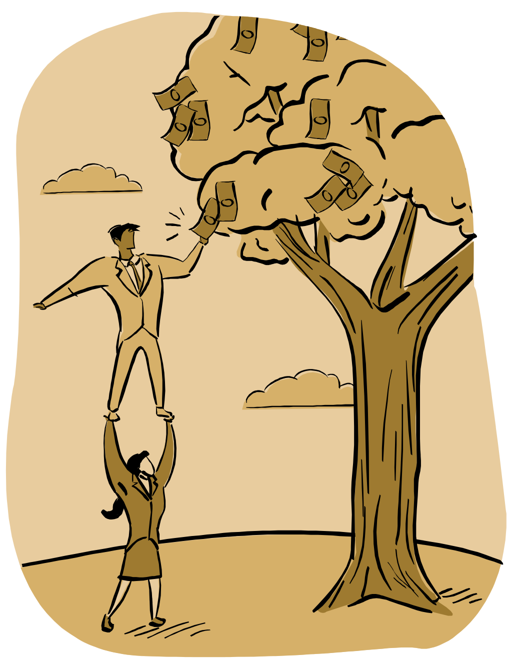
Conclusion

Convincing the business owner that the biggest threat to a business is that person's own mortality is tough. To many, the day to day challenges are enough to pull their boat asunder. Having a business succession or exit plan is critical to retirement, the succession of the business, and the continued financial well being of the owner. In the next segment, we will discuss potential heirs and follow through in the consecutive months on other important issues.

Dr. Bart A. Basi is an attorney, CPA, and the Senior Advisor of The Center for Financial, Legal & Tax Planning, Inc, a full service company specializing in financial, legal & tax matters. Basi is a nationally recognized author, lecturer, and advisor on how to structure deals to minimize taxes. Tax structure makes the difference between getting the deal done and watching the deal fall apart. Many of you may be familiar with Basi and the topics he covers in the Financial, Legal & Tax Advisory which may be read in various industry-specific trade publications.

Points of Interest

- **The number one threat to your continued going-concern is quite simply the lack of a business succession plan.**
- **Without succession planning, it is a near certainty a great portion of the business value will be lost if the "leader" passes away without a business succession plan.**
- **Having a business succession or exit plan is critical to retirement, the succession of the business, and the continued financial well being of the owner.**



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A CASE STUDY CONTINUED:

Editor's Comment: If the couple in this case had spent most of their time at their primary residence and travelled from this residence to various construction sites, they may have been able to deduct the travel expenses. But because the travel expenses they incurred appeared to be more by choice rather than necessary for the husband's work, they were not allowed to deduct them. To be deductible the expenses must be ordinary and necessary to generate income.

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Avoiding Common Mistakes in Selling Your Business – "If it ain't broke, don't fix it!"

Mike Ertel, CBI/ M&AMI/ CM&AA

Most buyers are eager to "make their mark" once they've acquired a business. But unless the business is losing money, or employees and customers alike despised the previous owner, it is generally a mistake for a new owner to make a lot of changes in the first 6 months.

Many times even small changes made with the best of intentions can have disastrous and unexpected consequences on employee morale and/or customer satisfaction, and ultimately on sales and cash flow. The risks are even greater if the previous owner was beloved by his employees & customers, as all eyes will be trained on you to see what waves you'll make -- presumed to be negative -- in this previous paradise.

If you're the new owner, most likely, you've just paid a substantial premium for the "goodwill" of this ongoing business. Respect this, and take the first few months to really get to know your employees and customers, who in reality are responsible for the business' continuing sales and cash flow. Get to know their true likes & dislikes about working in/buying from your business. Begin by making A FEW SMALL changes to remove their dislikes & reaffirm their likes, and then WATCH CAREFULLY how these changes affect employee morale, customer satisfaction, as well as top line & bottom line results.

If you know of a business owner who's thinking of selling or buying a business and who might benefit from a free, confidential, consultation with us, have them contact me at: mertel@legacyadvisorsgroup.com

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Frequently Asked Questions…

Q: I have a business which I would like to establish a value for. Is there a commonly used or well accepted formula or multiple I can use in order to value my business?

A: Quite simply, there is no easy way under the Internal Revenue Code or literature available to value a business in a proper manner using a simple multiple of revenue or formula. While there are various methods to value a business, qualitative factors must be considered along with the quantitative. If you are having your business appraised, it is best to deal with a trained professional to get a number where the business can be sold or valued for estate tax purposes depending on your situation.

Q: My sons are interested in being in business with me and are convenient successors. Should I assimilate them into the business as my successors?

A: Children are not necessarily the best successors to your business. While they can be a good succession plan to follow, it is best to weigh the situation. Sometimes it is best to sell the business to a third party or another business, or even a key employee. While parents want the best for their children, handing them an enterprise with responsibilities, cash, liabilities, and pitfalls everywhere may end up being an unmitigated disaster.

Q: If I desire to bring my children into the business as potential successors, is there any recommended course of action that will assure their successful assimilation?

A: The answer to this question is that no one course of action fits all situations. As a general rule, engaging the successors in the business and having them take business courses and technical courses is never a bad idea. At any rate, challenging, testing, and grooming them is a much better endeavor than a walk-in type succession.