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Planning for Business Succession

Business owners are often preoccupied with the day-to-day concerns of running and growing their companies, so **business succession** planning can often be overlooked, until it's too late. What would happen to *your* business if you were unable to work due to disability, or an unexpected death? Would your co-owners, managers, employees, and family members have the guidelines and tools in place to maintain your business?

Tips for Success

While there are many ways to approach succession planning, here are some basic steps to help you create a comprehensive plan:

1. **Start now.** Your family's financial future may depend on a sound succession plan. Get an early start, and follow the process through to completion.
2. **Assemble a team of professionals.** Because business succession planning involves many areas, obtain assistance from your team of qualified estate planning professionals, including your attorney, accountant, tax advisor, and insurance professional. They can work together as a team to help you develop a plan to achieve your objectives.
3. **If you want your business to continue after your death, choose an appropriate form of ownership.** The *form* of business you choose has tax, liability, legal, and business implications. If your business is established as a **sole proprietorship** or a **partnership**, it may be more difficult to transfer ownership after your death. To help ensure business continuity in the event of your death or incapacity, or that of one of your partners, consider converting to a **corporation**. Corporate status provides for the "perpetual existence" of the business, as well as limited liability for business owners.
4. **Choose and groom your successor carefully.** It is important to select a successor while you are still active because grooming your successor and familiarizing him or her with the finer points of your business may take years. Choose someone who can step into your shoes easily and help facilitate a seamless transition. A successful transition to new leadership depends equally on the person you select, as well as the training and experience you provide.

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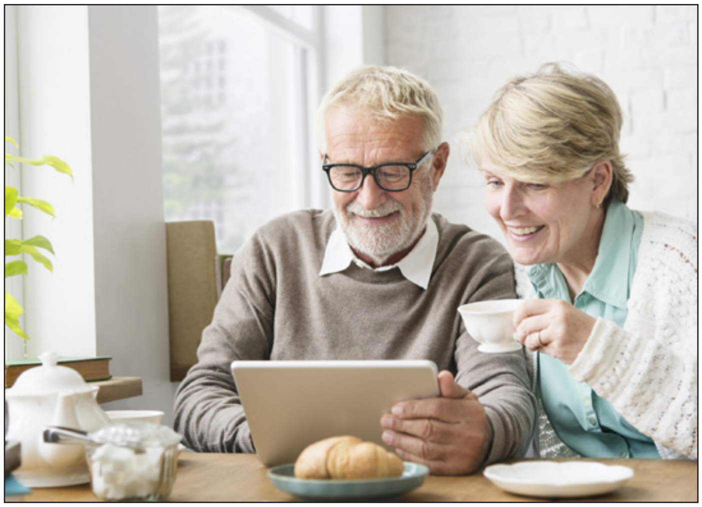
Understanding Retirement Plans

A pension plan is a means for providing income when an employee reaches retirement age and will no longer be working. If you work for someone else, you may be eligible to participate in an **employer-sponsored** retirement plan. If you are self-employed, it is your responsibility to set up and administer your own retirement plan.

For many employer-sponsored plans, eligibility is based on age and the completion of one year of service with the company. If a company is a corporation and offers a retirement plan, it will be either a **defined benefit plan** or a **defined contribution plan**.

A defined *benefit* plan provides the traditional pension. At retirement age, the company will pay the employee a fixed, lifetime income. The amount generally depends on the employee's highest attained salary and length of employment. Defined benefit plans are typically financed entirely by the employer. The employee generally pays nothing into this type of plan. The company assumes responsibility for ensuring that money is available to fund the benefit when the employee is ready to retire.

By comparison, a defined *contribution* plan does not provide a fixed lifetime pension. Instead, it requires that contributions (the employee's, the company's, or a combination of both) will be made to a retirement account in the employee's name. For example, a **401(k) plan** is a defined contribution plan in which the employee contributes a percentage of salary (on a pre-tax basis) and the company, at its discretion, may make a matching contribution. The company assumes no responsibility for the account. The balance of the account depends on how much is contributed annually and how the money was managed.



Whose Money Is It?

Vesting refers to an employee's *entitlement* to the funds in a plan. Generally, vesting is based on years of service with an employer. With a few exceptions, vesting rules are the same for defined benefit and defined contribution plans.

In a defined *contribution* plan, all employ*ee* contributions, and earnings on such contributions, are 100% vested from the start of participation in the plan. On the other hand, vesting for employ*er* contributions usually occurs over time. Should an employee leave a place of employment prior to retirement, he or she generally would be permitted to **roll over** the entire amount vested to date to another employer plan or to an **Individual Retirement Account (IRA)**. If allowed by the plan, the employee may leave the vested amount in the plan (to be drawn upon at retirement).

With a defined *benefit* plan, the commencement of benefits is determined by the terms of the plan. Although the employee accrues a vested benefit over time, the plan may specify that benefits will not commence until the employee attains **normal retirement age** (no later than age 65 or the fifth anniversary of the date when plan participation commenced).

Many defined benefit plans permit "early" retirement. However, an early retirement benefit may be reduced because the employee is expected to receive benefits over a longer period of time. If an employee leaves the company before normal retirement age, he or she could elect to receive an early retirement benefit if the age and service requirements (for early retirement) of the plan have been met.

In some defined benefit plans, a former employee will have his or her retirement benefit frozen. In that case, the employee generally cannot roll over benefits from one employer's defined benefit plan to another employer's defined benefit plan. Distribution of the employee's benefit will commence upon reaching normal retirement age. An individual with a frozen pension with a previous employer can contact the employer to find out how the retirement benefit will be calculated.

While neither plan is inherently better than the other, there has been a shift away from defined benefit plans toward defined contribution plans. Therefore, it is important to understand the risks and benefits between the two basic types of retirement plans.

Virtual Teams: Skilled Workforce Options for the New Economy

As more companies rely on the participation of employees and partners in geographically distant locations, "virtual team" building of individuals who meet online to work on projects or engage in business activities is increasing. To keep virtual teams connected and on course, companies need to implement the right networking and collaborative technology solutions, as well as develop innovative ways to encourage cooperation among workers who rarely, if ever, meet in person.

The Benefits of Virtual Teams

Companies may choose to create virtual teams for a number of reasons, including the following:

- Employees who are best qualified to contribute to a specific project or are best suited for a particular role are located in other parts of the country or the world.
- Global firms may need employees in multiple locations to cooperate and communicate with one another.
- Those employees looking for work-life balance or to save on commuting costs may want to work from home on a full- or part-time basis.
- Sales representatives who travel frequently as part of their job responsibilities must remain connected to co-workers and senior management while on the road.

Steps for Success

In order to facilitate information-sharing and encourage diverse ways of thinking among virtual team members, it is important that companies provide the technology needed for effective communication. Team members may require reliable Internet connections for smartphones, laptops, and personal digital assistants (PDAs) to remain productive, especially when traveling. Many individuals will use a combination of email, texting, and instant messaging to communicate with co-workers and managers, and to respond promptly to incoming messages. Team members may also be encouraged to maintain an online calendar to help the company keep track of their activities and schedule.

Document sharing and project management software programs can also make it easier for team members to effectively collaborate. These tools enable users to view any changes made and add their own contributions in real time.

While much of the work conducted by virtual teams can be done on a flexible basis, regularly scheduled meetings via phone or video conferencing are essential to remain productive. This provides team members with the opportunity to engage in a group discussion, airing any concerns they may have and connecting with one another on an interpersonal level. Team leaders may also organize interactive webinars for viewing online presentations. Some companies with large numbers of remote workers are experimenting with three-dimensional technologies in which avatars (graphical representations of the user, such as an icon or screen name) represent employees attending meetings and presentations in a virtual world.

Managers supervising virtual team members need to maintain contact with off-site employees and assess their performance on an ongoing basis. Rather than monitoring the amount of time each employee spends working, many companies choose to measure productivity by the results produced. This approach to management involves establishing clear objectives and requires employees to demonstrate that they are following schedules and meeting the goals set for them. It is equally important for managers to realize that capable employees who work independently may still need occasional guidance, and will also appreciate prompt responses to their communications.

If possible, virtual teams should be encouraged to meet face-to-face at least once a year at a social event organized by the company. This type of personal interaction can build trust among team members, as well as cultivate retention of a skilled virtual workforce.

planning for business succession

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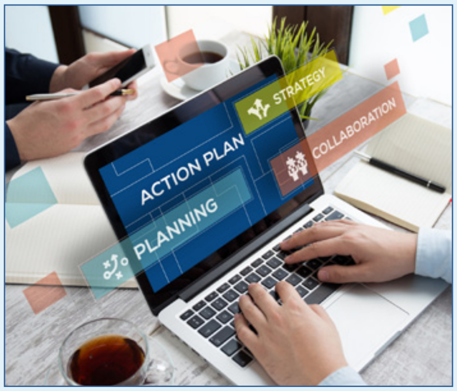
5. **Create a business "will" and a buy-sell agreement.** The business will is a comprehensive planning tool that can detail, in step-by-step format, your plans for the continuation of your business, including your management plan. In your business will, you may also name your successor.

   An important adjunct to a business will is a **buy-sell agreement**. A buy-sell agreement obligates one party to *buy* and the other to *sell* his or her interest in the business following a triggering event, such as the owner's death or disability. A buy-sell agreement can be structured as an entity purchase (redemption) agreement, a cross-purchase agreement, a hybrid (combination) agreement, or a "wait-and-see" agreement. Your planning team can assist you in selecting the most appropriate structure for your buy-sell agreement.

6. **Consider funding your buy-sell agreement with insurance to enable your chosen successor to buy the business.** Although a buy-sell agreement can help ensure that your business will remain with your family or business partners in the event of your death or disability, adequate funds must be available to meet the requirements of the agreement. **Life insurance** is a funding vehicle that can help ensure adequate liquidity should a qualifying event force the sale of an ownership interest. **Disability buy-out insurance** may also be purchased on the owners to fund the purchase of the business specifically in the event of a disability.



7. **Establish a dollar value for each owner's share.** For most small, closely held companies, it is not easy to put a dollar value on the business. You may need to obtain an independent appraisal of your business to help formulate your buy-sell agreement.

8. **Develop an estate plan to ensure adequate liquidity to help pay estate taxes and other final expenses.** Without prior planning, there may be no provision or funds available to pay estate taxes, which could be significant. You may want to consider purchasing enough life insurance to help cover the cost of estate taxes.

   In addition, consider **transferring** part of your business ownership to family members involved in the business using certain gifting or sale techniques. While relinquishing control of your business can be challenging, it can help reduce your assets, thereby reducing your potential estate tax liability.

9. **Discuss your plans with all involved parties.** By letting your family and management team in on your business succession plan, such as who will take over as owner and head of the company and why, you can help to minimize stress and confusion for your successor and your family.

10. **Review and update your succession plan as needed.** Once your plan is established, review it periodically with your team of professionals to address any changes that may be required. If a major change occurs in your business or personal life, review and revise your plan, as is necessary.

The time you take today to plan for business succession can help ensure that your wishes will be fulfilled when the time comes to transition into new ownership. Your family members and business associates will also benefit from your thoughtful consideration of their future needs.