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The Family Business Owner's Top 5 Business Succession Plan Considerations

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The typical family business owner spends his lifetime building the family business but spends insufficient time planning the successful business transition at his death. To increase the chances for a successful business transition, the business owner should implement the following strategies:

1. Groom successors. The owner must identify and groom his successor early and should communicate his plans to his successor, and to other management, employees or family members who will be affected. He should mentor his successor and foster her relationships with key vendors, lenders, customers, management, and employees. If there is no successor identified, then he should realistically assess the future of the business after his death. Will it be sold? Can other successors effectively step into ownership?

2. Continue business operations. The owner's death may impact the business' daily operations by interrupting relationships with vendors, lenders, customers, management, and employees, and decreasing profits. He should create a plan to address those concerns and test the plan before his death; in some cases, he should communicate the plan to those who will be impacted. The owner should also consider purchasing key-person life insurance to cover costs caused by his death, including hiring interim management, reducing debt, and bolstering revenue.

3. Protect family ownership. The owner who wants to retain ownership within his family must take additional action. To protect against his surviving spouse's remarriage, he may employ a marital trust to hold business interests. His children should implement antenuptial agreements to protect their business interests from ex-spouses. The interests of spendthrift children should be protected from their creditors by trusts. Buy-sell agreements should be implemented to prohibit transfers outside the family and facilitate the purchase of the owner's shares by his successors, and life insurance should be placed to fund those purchases.

4. Provide family fairness. If the successor is a family member, the owner should realistically consider how to fairly distribute his estate among the successor—giving due consideration to her efforts in the business' success—and the other children. Does fairness mean equality? Will the other children own shares of the business? If not, what assets can the owner leave them? If so, do the other children want to continue as minority shareholders? The owner's estate and gifting plans must carefully account for these dynamics and economic effects.

5. Minimize transfer taxes. When the owner dies, the business' value is taxable in his estate. If the value of his estate exceeds his available deductions and exemptions (currently $1 million for Minnesota taxes and $3.5 million for federal taxes), the combined tax rate is roughly 50 percent and taxes are due within nine months. While installment payments may be available, the owner should consider providing liquidity through life insurance held outside of his taxable estate in a trust. The owner should also implement a lifetime gifting plan to minimize transfer taxes on the passage of those assets to his family.