BUSINESS CONTINUITY PLANNING CONCERNS OF THE CLOSELY-HELD BUSINESS OWNER[1]

by Gary A. Olinger

Abstract. If you are the owner of a small, closely-held business, it is likely that your business comprises a most significant portion of your net worth and/or your income-producing capability. In that context, it is important to evaluate options available to you relative to this business enterprise in the event that you do not want or cannot physically maintain operational control over the business. Retirement, death, or prolonged disability of the major owner can dramatically impact a closely-held business. Planning for these eventualities in advance of their occurrence, therefore, is something no business owner can afford to ignore.

An owner of a closely-held business has basically one of three decisions to make relative to the disposition of his business interest in the event of his death, disability or living withdrawal (retirement) from his business. He can elect to keep the business, i.e., retain ownership for himself or his family, sell the business interest, or make no decision. Obviously, the first two decisions allow the owner to create a plan for the retention or sale of the business. To make no decision only defers to a later time and, perhaps, diverts to other individuals the responsibility of making the ultimate decision to retain or sell the business asset.

The purpose of this article is to explore the keep-sell decision and to evaluate factors which contribute to the planning strategy ultimately selected.

The Plan To Keep The Business

The impact of the decision to retain ownership of the business interest will vary — depending upon whether the event in question is the owner's death, disability or retirement. Table 1 summarizes some of the concerns that owners typically share when deciding to retain ownership of their business in these circumstances.

Needless to say there are potentially many other concerns that should receive focused attention when planning to retain the business asset but, at a minimum the business owner would be well advised to answer at least these eight questions if **keep** is his planning objective.

Planning techniques to assist the owner in his/her retention objective are too numerous to detail here. However, some which are common include:

Death planning.

1. *Recapitalize* the business. The owner retains Preferred Stock and the children receive Common Stock. Future appreciation is absorbed by the common stockholders, thus limiting the estate taxable value of the parents stock.
2. Execute a *will and trust* that specifically provides for business successor ownership and management, to include the power given to the trustee to retain the business as a working investment of the trust.
3. Provide adequate *liquidity* in the estate to pay due debts, taxes and expenses so as to avoid a forced sale of the business to raise the necessary cash.
4. Create an *"equilization" trust,* funded by non-business property, which can provide assets to family members who will not be actively involved in ongoing business management and control.
5. Maintain a program of *life insurance* which, when combined with other non-business property, will be sufficient to: a) provide the owner's surviving spouse and family adequate income, b) satisfy creditors if cash flow is interrupted by the owners death, and c) offer "keyman" indemnification to the business until successor management has gained necessary experience and expertise to assume the deceased owner's role.

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Disability planning.
1. Create a formal *Salary Continuation* program wherein the business would pay to the disabled owner-employee reasonable amounts of compensation during the months or years of disability.
2. Maintain individual and/or group *Disability Insurance* benefits — so as to provide the owner a base of monthly income without placing unnecessary strain on business cash flow.
3. Provide for *disability benefits* as an optional feature of the company's qualified *retirement plan.*

Retirement planning.
1. Take advantage of deferred compensation techniques which allow significant tax-deductible deposits to accumulate on a tax-deferred basis until the owner's retirement, at which time retirement plan income can replace earned compensation.
2. Provide incentives for key personnel to remain active in the business after the owner's official retirement. Incentives might include individually designed fringe benefits (ie. nonqualified deferred compensation to be paid to the key person at a target date), officer status, stock appreciation rights (future compensation related to improvement in the net worth of the company), and interest free loans from the company to the key person.
3. If the business is a Corporation, the election to have Corporate profits taxed directly to the shareholder (Sub-S election) allows the retired, inactive business owner to receive dividends from the company without exposing them both to Corporate and Personal tax brackets. Also, the owner need not be employed to justify this income.

The Plan To Sell The Business

Closed corporations and partnerships, in which the personal services of the owners are essential to the success of the business, are normally formed or entered into because of the particular skills and personalities of the parties. Naturally free substitution or transfer of ownership is sometimes not only undesirable but potentially dangerous to the successful ongoing operation of the business.

For this and other reasons, the decision to keep the business is not always wise, nor practical. The alternative is to create a plan to **sell** the business

Table 1. Concerns to share when deciding to retain ownership.

Concern	*Death*	*Disability*	*Retirement*
1) Source of income when owner is no longer fully employed?	X	X	X
2) Who will manage the business in owner's absence?	X	X	X
3) How will the owner's departure from day-to-day management affect:			
Profits?	X	X	X
Customer relations?	X	X	X
Creditor relationships?	X	X	X
Employee morale?	X	X	X
4) How will the business be valued for estate and inheritance tax purposes?	X		
5) Where will the liquidity come from to pay federal estate taxes and other expenses associated with the death of the owner?	X		
6) Will the business be able to pay its debts in a timely manner?	X	X	X
7) How will minority shareholders be affected?	X	X	X
8) If the business is retained for certain family members (i.e. working son of owner), how will asset distribution be equalized to other family members?	X	X	X

asset, in part or in its entirety, when the owner is no longer actively employed. Again, this decision triggers a number of planning questions, the answers to which can form a meaningful track on which to build the plan to sell the business assets:

1. Should there be a written agreement? (i.e. purchase and sales or "buy-sell" agreement)
2. Who should be the buyer?
3. What should be the purchase price?
4. How should the purchase price be paid out (terms)?
5. How will the buyer obtain funds for the buyout?
6. In what events should the buy-out take place (death, disability, retirement, or other living withdrawal)?
7. What will be the tax affects to the buyer/seller?
8. Should the agreement "peg" the business value for estate tax treatment (death buyout)?
9. How will the proceeds of the buy-sell be invested?
10. Should the buy-sell agreement contain non-compete clauses?
11. Following the sale, who will control the business?
12. Should insurance assets be utilized to fund the agreement in the event of a death or disability? How about the use of a sinking fund?
13. How will creditors of the business impact upon the satisfactory completion of the buy-out?
14. Should the buy-out be optional or mandatory on the part of the proposed buyer/seller?
15. How should the agreement reflect future changes in the value of the business?

A well conceived purchase and sales agreement considers each of these questions, among others, and attempts to provide meaningful answers through its well-drafted provisions. Lucky is the closely-held business owner who, having decided to sell his business at his death, disability, or retirement, can establish a ready market for his interest, obtain a fair value, and be able to plan on the cash being there when it is needed to fulfill the terms of the buy-out.

The difference between *liquidity* and *liquidation:* this is the result of a well planned buy-sell agreement!

Keep? Sell? No decision? What plan do you have, and how well prepared are you for its execution?

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ABSTRACT

SKELDING, MARK. 1983. **European pine shoot moth may pose new problems for bristle-cone pines.** Am. Nurseryman 157(7): 89.

European pine shoot moth (*Rhyacionia buoliana*) has been observed feeding on bristle-cone pine (*Pinus aristata*), a previously unrecorded host, at The Dow Gardens, Midland, Michigan. *P. aristata* is considered relatively pest-free, with dwarf mistletoe one of its few commonly reported pests. European pine shoot moth is a common shoot borer that can cause extensive damage on ornamental conifers. Its hosts include many pines, particularly Scotch, red, and Austrian pine. Dead or deformed shoots are common symptoms. *P. aristata* is currently being introduced as an ornamental to the Great Lakes States. It appears to be adapting well. It is native to the mountainous regions of the Southwest and suited to dry, well-drained, low-nutrient soils. This adaptability, along with its compactness, picturesque habit, longevity, and pest resistance makes it desirable for landscape use.