Business Continuation Planning Issues

Have you considered the impact your death or disability could have on the value of your business, and on the stream of income upon which you and your family depend?

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Real Value of Your Business

What Is the Real Value of Your Business to You and Your Family?

If you're like most business owners, ownership of a business has provided you with the opportunity to build an asset of considerable value...an asset that also generates a stream of income upon which your lifestyle and that of your family is dependent.

BUT...

Have you ever considered the impact your death or disability could have on the value of your business, and on the stream of income upon which you and your family depend?

Planning Considerations

Consider...

- If you had died or become disabled yesterday, who would own and operate your business today?
- Would your business be able to continue an income to you if you became disabled?
- Would your business be in a position to continue an income to your family in the event of your death?
- Would your estate have sufficient liquid assets to pay estate taxes and other estate settlement costs?

Without Advance Planning, the Facts Are...

- A small business may be forced to liquidate at an owner's death or disability; or
- The business may have to be sold, often at a greatly diminished value.

Business Continuation Options

The Three Business Continuation Options:

In planning to preserve the value of their business interests at an owner's death or disability, small business owners have three alternatives to evaluate:

Retain the Business for the Family
Sell the Business to Co-Owners, to an Employee or to an Outsider
Liquidate the Business on a Planned Basis

The objective of **business continuation planning** is to assist you in evaluating which of these alternatives is most suitable for your situation and to help provide the funds that will be needed to assure that your business continuation goals become a reality.

Retain the Business for Family

Without a capable family member to continue the business, it can be difficult to preserve the value of a small business interest UNLESS a market for the business is created PRIOR to the owner's death or disability.

When your objective is to retain your business for your family, these are some of the issues you must consider:

- Which family member(s) will own and manage the business?
- Will this family member be acceptable to any other owners?
- How will the business interest be transferred...by will, gift or sale?
- Will this method of transfer create a need to equalize inheritances among heirs?
- In the event you are disabled, will the business need to continue an income to you? Will the business need to continue an income to your family in the event of your death? Will funds be available for this purpose?
- Do you know the value of your business?
- Will there be sufficient liquidity in your estate to pay estate taxes and other settlement costs without liquidating business assets?
- Will there be a period of decreased profits during the transition to new management?
- Will credit lines be disrupted or outstanding loans have to be repaid?

When the objective is to retain the business interest for the family at an owner's death or disability, funds may be needed:

- to pay estate taxes and other estate settlement costs.
- to continue an income to the disabled owner or surviving family.
- to equalize inheritances among heirs.
- to provide additional working capital during the transition to new business management.

Sell the Business

When your objective is to sell your business, these are some of the issues you must consider:

- To whom will your business interest be sold...a co-owner or owners, a key employee or an outsider?
- At what events will your business interest be sold...death and/or disability?
- What is the value of your business interest? What would a willing buyer pay for your business? For how much would you sell your business?
- What will be the source of the funds needed to complete the sale?

When a potential buyer for a small business interest can be identified...a co-owner, a key employee or an outsider...advance planning can provide:

- a ready market for your closely-held business interest.
- a predetermined price at which the buyer will purchase and you will sell your business interest.
- the funds to complete the sale at your death or disability.
- an established business value for estate planning purposes.
- the peace of mind that comes with knowing you have preserved the value of your business interest.

Liquidate the Business

Unfortunately, in some situations there is no capable family member willing to continue the business and a willing buyer cannot be identified. In these situations, the only alternative may be to liquidate the business at the owner's death or disability.

Without proper advance planning, however, a financially-disastrous forced liquidation may result. A forced liquidation can greatly diminish the value of the business asset, while eliminating the source of income upon which the owner or surviving family depended.

When your objective is to plan for the orderly liquidation of your business at your death or disability, these are some of the issues you must consider:

- What is the value of your business if it could be sold as a "going concern?"
- What is the liquidation value of your business, if liquidated on a planned basis?
- Do you want to offset the diminished planned liquidation value of your business?
- What cash and income needs must be satisfied to allow for a planned liquidation of your business at your death or disability?
- How will the funds be provided to allow for an orderly liquidation of your business?

When a business cannot be retained by the family or sold at an owner's death or disability, advance planning can enable a planned, orderly liquidation of the business by providing the funds needed:

- to pay estate taxes and other estate settlement costs.
- to continue an income to the disabled owner or surviving family.
- to allow the time for a planned liquidation that maximizes the liquidation value of the business.
- to offset the diminished value of the business that results from even a planned liquidation.

Estate Planning Considerations

Whatever your objective – to retain your business interest for your family, to sell your business or to liquidate your business on a planned basis – your plan also must take into account certain estate planning considerations.

The federal estate tax is a **progressive tax on the right to transfer property at death**. In 2019, federal estate tax rates begin at 18% and increase to as much as 40% of the taxable value of an estate.

The **federal estate tax** is a transfer tax imposed on the privilege of transferring property at death, while the **federal gift tax** is imposed on the transfer of property during the property owner's lifetime. Both taxes are levied on the **right to transfer property**, and not on the property itself. The amount of tax payable, however, is measured by the **value** of the transferred property.

Once the tentative federal estate or gift tax is determined, it is then reduced by an **estate and gift tax unified credit**. This means that **taxable estates with a value equal to or less than the unified credit equivalent** will not be liable for federal estate tax. The same is true of **cumulative lifetime taxable gifts** which, however, will be brought back into the owner's estate for federal estate tax calculation purposes. **The unified credit equivalent is equal to $11,400,000 in 2019, as adjusted for inflation**, meaning that an individual currently can transfer property valued up to $11,400,000, whether during life and/or at death, without incurring a tax liability.

In addition, **"portability" of the maximum estate tax unified credit between spouses** is available, meaning that a surviving spouse can elect to take advantage of any unused portion of the estate tax unified credit of his or her predeceased spouse (the equivalent of $11,400,000 in 2019). As a result, with this election and careful estate planning, married couples can effectively shield up to $22 million plus (as adjusted for inflation) from the federal estate and gift tax.

Finally, **estate tax deferral** allows payment of estate tax attributable to the value of a closely-held business included in the estate to be deferred for up to five years.

No discussion of estate planning considerations in regard to business continuation would be complete without mention of the **generation-skipping transfer tax** (GSTT). An objective of the federal government is to collect taxes on the transfer of property from one generation to the next generation. If, however, an estate owner is able to skip the members of the immediately lower next generation and transfer property to someone two or more generations removed, the government is deprived of the estate tax that would have been collected on that property at the death of members in the immediately lower next generation. As a result, a generation-skipping transfer in excess of available exemptions is subject to the maximum federal estate and gift tax rate of 40% in 2019. The GSTT is **in addition to** any federal estate or gift tax due and is payable by the transferor, the transferor's estate or by the trustee of a trust making a generation-skipping transfer.

> Your professional tax advisor can assist you in developing business and estate plans with the flexibility needed to adjust to an uncertain tax future.

Odds of Becoming Disabled

Are you willing to gamble your financial security and that of your family on these odds?

Age	Number of Business Owners				
	1	*2*	*3*	*4*	*5*
30	54%	79%	90%	96%	98%
35	50%	75%	88%	94%	97%
40	45%	70%	84%	91%	95%
45	40%	64%	78%	87%	92%
50	33%	55%	70%	80%	86%
55	25%	43%	57%	68%	76%

Source: Commissioners Individual Disability Table A (NOTE: The 1985 CIDA is the most current morbidity table available for individual disability claim experience and is in use by many State Insurance Departments.)

It's also important to know that a disability lasting for more than 90 days is likely to continue for:

Age When Disabled	Average Duration of Disability
30	2.2 years
35	2.5 years
40	2.7 years
45	2.9 years
50	2.8 years
55	2.5 years

Source: Commissioners Individual Disability Table A (NOTE: The 1985 CIDA is the most current morbidity table available for individual disability claim experience and is in use by many State Insurance Departments.)

Odds of Dying

What Are the Odds of an Owner Dying Prior to Age 65?

Here are the statistical chances of death prior to age 65 of owners in a business. Column one shows the chances if there is just one owner; column two shows the chance of one death when there are two owners; column three shows the chance of one death when there are three owners.

One Owner		Two Owners		Three Owners	
Owner's Age	***Chance of Death***	***The Two Owners' Ages***	***Chance of Death of One Owner***	***The Three Owners' Ages***	***Chance of Death of One Owner***
30	28%	30, 30	48%	30, 30, 30	63%
35	27%	30, 40	47%	35, 40, 50	58%
40	26%	30, 50	44%	40, 40, 45	59%
50	22%	30, 60	36%	45, 45, 45	57%
55	18%	35, 40	46%	50, 50, 50	53%
60	17%	40, 45	44%	30, 35, 60	54%
		45, 45	43%	35, 40, 40	60%
		40, 55	39%	30, 55, 60	48%
		50, 50	39%	40, 55, 60	46%
		50, 60	31%	45, 55, 60	45%
		60, 60	22%	50, 50, 50	53%
				55, 60, 60	36%

Source: Commissioners Standard, Mortality Table

A few hours spent in business continuation planning can turn uncertainty into certainty...for you, your family and your employees.

Important Information

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