

Lifetime Planning Can Help Keep Your Business Safe and Sound for Your Heirs

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For many business owners, the dream of someday handing down a successful business to their children has fueled years of hard work and sacrifice. Making that dream a reality, however, requires a combination of careful planning and avoiding the potholes along the way. Often the day-to-day concerns of running the business push aside the centrally important task of preserving the business for children and grandchildren.

Without proper planning, much wealth can be lost to taxes, employee theft, litigation, failed relationships and disputes among owners. The good news is that many of the pitfalls are foreseeable and advanced planning can decrease the likelihood of a catastrophic loss.

This article is the first in a two-part series that discusses lifetime and estate planning for business owners. Part one discusses potential

threats to the business during the owner's lifetime and suggests tips that may be useful in avoiding or minimizing the impact of these threats. Part two (to appear in the September/October issue) discusses threats that may arise following the owner's death and offers planning suggestions to be implemented during the owner's lifetime to address these threats. Although these articles speak in terms of a business owner, many of the issues are applicable to professional practices as well.

Tip No. 1: Avoid Sole Proprietorships and General Partnerships

The form of business you choose can determine whether your personal assets are subject to the claims of business creditors. Sole proprietorships and general partnerships offer no protection to the owners' personal assets against business debts. Corporations and limited liability companies (LLCs), on the other hand, can provide an effective shield against most creditor claims, but only if the corporation or LLC is properly funded and maintained. LLCs and "S" Corporations provide these benefits with little or no adverse tax consequences. [An "S" Corporation is an ordinary corporation that has qualified for and made a special IRS election under Subchapter S of the Internal Revenue Code.]

Historically, limited partnerships and "S" Corporations were most widely used for small businesses; however, LLCs have grown in popularity and acceptance over the last few years and are quickly becoming the entity of choice. LLCs are suitable for businesses with one or multiple owners, as are S Corporations.

The good news is that forming a corporation or LLC has never been easier. The Georgia Secretary of State's office has very recently begun accepting electronic filings. What once took days and weeks can now be accomplished in one day. Existing unlimited liability business-

es that started off as sole proprietorships or general partnerships may now be quickly converted to a limited liability business.

Tip No. 2: For Multiple Businesses or Multiple Properties, Don't Stop at One Corporation or LLC

Part of preserving and protecting wealth involves using layers of entities. If your business has multiple operations, business lines or properties, it may make sense to put each in a different entity so that all of your business assets are not subject to the claims of one business line or investment. For example, your operating business might be in one entity, the office and real estate in which your business is housed might be in another. Your entity that owns the real estate would then lease it to the operating entity. This may also create opportunities for you to begin making gifts of interests in the real estate or the business during your lifetime to your heirs.

Tip No. 3: Respect the Entities You've Formed

Having a corporation or LLC doesn't help you if the entity is not properly funded or maintained. Businesses should be given adequate capital to begin and maintain operations. Corporations should have regular meetings of the board of directors and shareholders, with written minutes taken and placed in the corporate records. Business assets should not be mingled with personal ones. Business checking accounts should not be used to pay personal bills. Contracts should be signed in the business's name, not the owner's individual name. Annual fees and filings imposed by the Georgia Secretary of State's office are not onerous; however, they need to be paid and made. If you fail to respect the corporate entity, a plaintiff may

be successful in having the entity disregarded, which can then subject your personal assets to business claims.

Tip No. 4: Make Sure You Have Enough Insurance

Rather than relying solely on the protection afforded by an entity (which, as we've seen above, can be lost), you and your business should purchase adequate liability and hazard insurance. A knowledgeable, trusted insurance advisor can meet with you to select the types and amounts of coverage you need to protect your business and your family. Umbrella policies are frequently available at a comparatively small cost to minimize the risk of a catastrophic claim in excess of regular coverage.

Tip No. 5: Choose Your Partner Wisely, if At All

Most businesses are best served by not bringing in third parties as partners or co-owners. Once someone has been made a co-owner of the business, that person is granted a variety of rights under laws that are not applicable to mere employees. Removing a partner is much more difficult than firing an employee. If your goal is to reward an individual for a company's performance, there are ways to accomplish this through salary, benefits and bonuses without making that person an owner.

If you wish to bring in a partner, you should work carefully with an outside advisor to address up front and in writing what will happen should the relationship not survive. Similarly, if you make gifts of business interests to a family member, you'll want to address what happens upon death or divorce of the family member so that you don't suddenly find yourself in partnership with an ex-spouse or ex-son-in-law.

Tip No. 6: Choose Your Employees Carefully

Often the biggest threat to a business is not a third party claim, it is theft by a trusted employee. Proper screening, background checks and obtaining references from previous employers are necessary steps. In addition, you should put into place financial controls to minimize the likelihood of theft. A system of checks and

balances may deter and prevent employee theft and increase the likelihood of discovery should theft occur. Unfortunately, once the theft has occurred, recovering the amounts taken can be very difficult and expensive, if not impossible. Deterrence and prevention are the keys. Your accountant should be able to assist you in crafting the controls, checks and balances.

Tip No. 7: Choose Your Spouse Carefully

Statistically, divorce rates are said to approach 50% on a national basis. The divorce rate for second marriages may even be higher. If you're an established business owner considering marriage or remarriage, you should look carefully at whether to put in place an antenuptial or prenuptial agreement. These types of agreements will specify what happens to each spouse's separate assets and the marital assets on death or divorce. To aid in enforceability, each spouse should have his or her own lawyer, all attachments to the agreement should be included and the agreement should be followed once the marriage has taken place.

Tip No. 8: Plan for Disability As Much As Death

For many age groups, the statistical likelihood of a temporary or permanent disability prior to age 65 is greater than a premature death. Many business owners will buy life insurance but will fail to plan for disability. Because a disability may carry with it extreme costs, steps should be taken in advance, such as the purchase of disability insurance.

Tip No. 9: Have a Succession Plan

Although stories abound of inexperienced spouses and children stepping up at the owner's death, only to have the business thrive as never before, the sad reality is that most family businesses without a clear succession plan suffer dramatically at the owner's death. Great value in the business can be lost if untrained survivors are forced to sell or liquidate the once-successful business now reeling from the owner's death. Succession plans will be more fully discussed in part two of this article.

Family members who will be called upon to run the business following the owner's passing

should be cross-trained in each area of the business to obtain the necessary expertise.

Tip No. 10: Pay Attention to Applicable Laws, Particularly Wage and Hour Laws

The Fair Labor Standards Act is the federal statute that sets the minimum wage and provides generally that employees must be paid overtime when working in excess of a 40 hour week. While exceptions from the overtime requirements do exist (such as the exception for true managerial employees on salary), these exceptions are narrowly construed. Merely labeling an employee as "managerial" or as "salaried" will not alone defeat the employee's right to overtime. Penalties and back pay owed can be dramatic. Wal-Mart Corporation recently agreed to pay \$33.5 million plus interest to settle overtime claims with the US Department of Labor.

Conclusion

Many business owners share a dream of passing down their business to the next generation. However, in order to have something to pass down, the business must survive the threats and challenges along the way. Careful planning can lessen the likelihood of loss and help fulfill the dream. Next time, we'll talk about steps you can take so that the business and other assets you've worked so hard to preserve and maintain may be passed down to your heirs.

About the author: Richard E. Barnes is a Valdosta attorney, speaker and author specializing in business and estate planning for business owners and professionals. Richard is the author of "Till Death Do Us Part (Again): Estate Planning for Second Marriages", recently published in the March/April issue of the American Bar Association's Probate & Property Magazine. Richard is a shareholder with Elliott, Blackburn, Barnes & Gooding, P.C., in Valdosta, Georgia. For more information, see www.ebbglaw.com.

How protected are you?
Turn the page and take the quiz to find out

Lifetime Planning Quiz

How protected are you? Take the quiz!

1. My corporate minute book

- (a) Is accurate and up to date
- (b) Is holding up one corner of the copier
- (c) Was last seen during the Ford administration

2. My agreement with my business partner

- (a) Is spelled out in a shareholders/partnership agreement
- (b) Is spelled out on the back of a Wooden Nickel napkin
- (c) Is more of an agreement not to disagree.

3. My plan for an unexpected disability

- (a) Is addressed by insurance, regularly reviewed to ensure amounts are up-to-date
- (b) Is a bullet, a bottle of whiskey and an iron will to work through whatever it is
- (c) Involves experimental cloning and creation of my twin

4. Insurance

- (a) In the right amounts, written by the right carriers in consultation with the right advisors, can be invaluable
- (b) Is for the weak
- (c) Is for those who don't know how to drive

5. My partner and chief financial officer

- (a) Pays all of our bills, including taxes, on time
- (b) Is here for a good time
- (c) Is currently doing time

6. When in doubt I

- (a) Call a trusted advisor
- (b) Use the Gomer Pyle test-taking method (bang two fingers on the table, go with the one that's tingling)
- (c) Hide in the corner

7. My succession plan

- (a) Has been carefully thought through, reduced to writing, and communicated to my children whom I am grooming to take over
- (b) Involves the Vatican, the College of Cardinals and two colors of smoke
- (c) Is to live like I was dying, but avoid the dying part

8. I am getting remarried. I have substantial means. My potential husband's most valuable possession is a 1979 Dodge

Ramcharger. I should

- (a) Request that he sign an antenuptial agreement (prenup) prior to our wedding
- (b) Request that he sign over the Ramcharger to pay for our wedding
- (c) Request that he stop calling me "sweet thang" in front of my board of directors.

Give yourself 5 points for each (a) answer, 2 for each (b) and 0 for each (c).

How did you score?

25-40: Great job! Let's do some fine tuning.

15-24: Good job! Some work to be done, you'll get great improvement quickly.

0-14: Roll up your sleeves and let's get to work, you (or your spouse or your children) will be glad you did.