

Passing the Torch-Succession Planning

Picture this... A dealer (father) is in his mid-60s and has been in business for 25-years as a single-store operation. A key employee (son) in his middle-30s has been in the business for 10 years and shows great promise. The major supplier informs the dealer that he will either be a buyer or a seller of the business in the next five years. The dealer remains in good health, has two other children, is considering retirement and has confidence in his son.

Sound familiar? If so, read on. Samuel Kreamer, J.D., C.P.A. of Kreamer Law Firm, P.C. offered numerous tips and suggestions on succession planning during his session titled, "Passing the Torch."

Keys to Success

First, Kreamer stressed the importance of assembling a proper team. This team should include the dealer and an advisory team made up of his/her attorney, accountant, bankers/financial advisors, family therapist/counselor and I-NEDA.

Kreamer encouraged dealers to make advance preparations and lay the groundwork. He recommended they:

- *Define the Plan* – Determine retirement objectives and identify potential buyers/sellers.
- *Perform a Complete Internal Audit* – Review key corporate documents with non-owner and owner. Evaluate internal systems and capabilities.
- *Review Financial Statements* – Prepare financial statements, remove non-operating assets and evaluate financial results.
- *Hold Meetings*

Kreamer also discussed the general concepts of retirement/deferred compensation and the use of life insurance to fund deferred compensation. He also covered the tax considerations and mechanics involved.

The "Art" of the Deal

Once a dealer identifies external and internal candidates, it's time to put together the deal. Kreamer reminded dealers that the deal is a process, *not* an event. The normal steps in a deal include:

- *Initial Meeting* – Kreamer referred to this step as the "introduction" – a chance for the parties to "measure" each other. He reminded dealers that the Association can help facilitate this process and act as a neutral party.
- *Confidentiality Agreement* – According to Kreamer, this is the "dating" period. While this important step allows access to confidential information, it also restricts the uses of the information.

- *Letter of Intent* – “The falling in love stage.” The letter’s content includes the basic structure, pricing and closing information.
- *Contract* – “The engagement period.” The contract is traditionally very long and detailed. It sets out price, terms and conditions, and addresses representations and warranties. Kreamer discussed setting the price using either the balance sheet approach or income statement approach. He also compared the types of buy/sell agreements – mandatory/permissive or cross purchase/redemption.
- *Closing* – “Marriage”

Gain Exclusion Rules and the Family Business Deduction

Kreamer detailed gain exclusion rules (section 1202) for non-corporate taxpayers and the family business deduction (Internal Revenue Code Section 2057). Gain exclusion rules stipulate that half of the gain on stock is excluded; the stock must have been issued after August 10, 1993 and held for more than five years; and it must be a “small business stock.”

On the other hand, the family business deduction:

- Is applicable to estates of decedents dying after 12/31/97.
- Is formerly designated Internal Revenue Code Section 2033A.
- Includes no regulations.
- Is applicable to “Family Businesses.”
- Provides a substantial deduction to facilitate the intergenerational transfer of the family business.
- May cause family business owners to revise their estate plan.
- Increases the importance of “grooming” the “successor.”

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