FINANCE 301

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My Knowledge Transfer Plan

Chapter 5: Estate planning and business succession.

I got my start in the financial services world by selling life insurance across the kitchen table to young families. Once, as I met with a 20-something couple, the husband told me it was ironic we were meeting because they had just found out the day before that his wife was pregnant.

Sensing an opportunity, I immediately started to explain a family life insurance policy that offered coverage on the husband, the wife and any and all children once they were born. The premium was $25/month, however, which was a lot of money for a young couple in 1980. The husband said, "We will probably wait on this until the baby is born."

In hindsight, I now understand why my reply caused them to evict me from their home: "Why wait? Do you want to see if you like the baby?"

During my career, I have encountered many clients who wanted to wait on their estate and business succession planning needs until "later." How ridiculous! These things can be amended, but as the old Yiddish expression goes, "Man plans, God laughs." Once you own a business, you must make estate and succession planning decisions. You have debts to pay and non-liquid assets that control your wealth. I don't care if you are young, old or really old – this is not something to be postponed.

Basic estate planning involves transferring assets from one party to a surviving party. Most people make this transfer via a will, but property transfers can occur in one of three ways:

• *Operation of Law* This is the way you would title an asset. Joint titling, for example, means that upon the death of one of the titled parties, the asset automatically flows to the surviving party. This does not require a will; it happens automatically by presenting a death certificate to the bank or county. In fact, even if someone's will states that the property interest should go to another party, it doesn't matter! Most real estate and many bank accounts between couples are set up this way. Stock in a business, however, is not set up using joint titling.

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• *Contract* This is the way most life insurance is set up, with a named beneficiary. Life insurance is a contract between the policy owner and the insurer. Upon the death of the insured (usually the policy owner), the proceeds go automatically to the beneficiary. As you have undoubtedly seen when payment of a funeral bill involves insurance, once death occurs, the proceeds can only be paid to someone else if the beneficiary agrees to it since it is the beneficiary's money at that point.

• *Probate* This is the default method that goes into effect if the two other methods are not used. If the deceased did not arrange to transfer an asset to a survivor by operation of law or via a contract, then it goes through probate. Ideally, probate involves a will, which will show how the deceased wanted the assets distributed. In the absence of a personalized will, however, the state draws one up for you. That will is called "intestacy," and each state sets the order of who will inherit property based on their legal relationship with the deceased.

A MATTER OF TRUST

I frequently hear people say, "We have a trust that will handle that." A trust is a contract, and the trust will either own the property during an individual's lifetime or after the property is transferred to the trust upon death. The trust will also have members of a team who make decisions. The trustee is in charge of managing the assets, and either the beneficiary is the recipient of the income (aka "income beneficiary") or the trust might distribute the property to someone at some point (aka "remainderman").

A trust is not omnipotent, however. Trustees are usually not good at running businesses unless they have experience running businesses. Running a funeral home is very complex and requires hands-on management. Think about who you can trust to make day-to-day decisions for your business.

A trust is a great tool when properly thought out. If you decide to create one, you can put it in place during your lifetime, but the assets should be titled in the name of the trust.

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During your lifetime, you would probably want to be the trustee and make all the decisions concerning the trust assets. This is called a "living trust" or "inter vivos" trust (meaning "between the living"). You would probably be the income beneficiary as well and receive all the income generated by the assets of the trust. Upon your death, there would be a contingent trustee and contingent income beneficiaries.

The trust might have provisions for tax reduction or might just be used for management purposes. This was more popular in the past, but for the past decade, the estate exclusion has provided no tax due on the federal level for most decedents. Only 0.2% of all estates pay a federal tax. For the 2021 tax year, the federal estate tax exemption is $12.06 million for an individual and $24.12 million for a married couple.

There may be estate or inheritance taxes at the state level as the states can set their estate transfer tax at different thresholds. About 17 states have estate or inheritance taxes, and most apply a tax above $5 million.

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DON'T SPLIT THE BABY

Too often, funeral home owners just "split the baby" by giving ownership to *all* of their beneficiaries. As an expert witness in litigation cases, I love seeing business owners abdicate their decision making like this because it usually leads to litigation between those wanting to be the successors and those in the family who just want the money.

Seriously! Imagine that you owned a Stradivarius violin and that it's the primary asset of your estate. Now suppose you have three kids, but only one has chosen a career playing the violin. Would you leave this instrument equally to all three kids? Of course you wouldn't. Likewise, if you have multiple kids but only one/some have chosen the funeral business as their career, I hope you won't leave the business to all of them.

Perhaps you're thinking of getting creative and leaving the business to some of your kids and the real estate to the kids not active in the business. Don't do that either! The kids running the business need to control the real estate, both for the sake of their wealth and perhaps for future growth needs. If the kids not active in the business own the real estate, then they will want income from rents, and negotiating those rents can cause fights. Can you possibly run a funeral home out of the trunk of a car? Just as controlling the real property is important to you, so, too, will controlling the real estate prove critical to the kids or key people who want to be your successor.

It is best to sell the business to the kids in the business during your lifetime. Your estate then becomes liquid, and you can easily divide an estate made up of cash, while an estate comprising non-liquid assets

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A great exercise to go through now, while you're healthy, is to write out your job description. Then gather your staff and ask, "If I am hit by a bus, who is going to do these tasks?"

is difficult to divide. Or, if you don't make that sale during your lifetime, then do it at the time of your death by having the kids who are active in the business sign a buy-sell agreement. This way, they can get an appraisal and buy the business (and the real estate) from the estate. Once again, the estate then becomes liquid and easy to divide.

A great exercise to go through right now, while you're healthy, is to write out your job description. Once that's done, gather your staff and ask, "If I am hit by a bus, who is going to do these tasks?" Not only is this important in case you do get hit by a bus, but it also helps you assess whether there is a contingency plan for your business. If you do not receive a complete demonstration that the business can continue in your absence, then it's time to start building that contingency plan.

Estate and business succession matters are akin to driving a car. Upon entering your vehicle, you put on your seat belt, but you don't wait to latch it until you see an accident about to happen! It is better to have your business succession plans in place, as a contingency, than to be on your deathbed wishing you had signed them.

Dan Isard is founder of The Foresight Companies, which has served thousands of funeral homes nationwide for the past four decades. The articles in this series can be found on the Insights section of theforesightcompanies.com. *Contact Isard at 602-274-6464 or danisard@theforesightcompanies.com.*