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Plan Ahead to Help Ensure Your Business Survives Future Generations

I truly enjoy hearing the stories from entrepreneurs and visionaries who have worked for decades to create their businesses. These businesses become like children to them and a large part of their essential self. As such, it is understandable that so many would like their entire family to remain intact—children and business.

Even if you're not ready to pass the torch, it is crucial to start planning now to help ensure a smooth transition and avoid the pitfalls along the way. It's estimated that 70 percent of family businesses will not survive into the second generation. To be among the 30 percent that do survive to future generations, or better yet, to grow that 30 percent, let's see what you can do.

Why do so many successful business people fail at the essential task of planning to pass their business on to the next generation?

The reasons may include fear of losing control, unwillingness to develop a succession and estate plan (for financial or political reasons), or difficulty in choosing a successor, which can be complicated, especially when family members are involved. As a result, many business owners adopt a wait-and-see attitude or simply tell themselves that everything will fall into place naturally.

Waiting until you are "ready" to retire to create a succession plan can be disastrous. An untimely illness may leave the business without a leader before others are prepared to step up. Most professional advisers agree that you should plan for a 3- to 5-year transition phase to allow your successors to build the skills and acquire the experience they will need.

Common Considerations in Succession Planning

1) Understand the future generation's vision for the business

If you impose your views on family members who are active in the business without listening to theirs, it may lead to distrust and misunderstanding and a more difficult transition.

2) Start thinking about various compensation models

Consider how to fairly compensate each family member in their roles. For example, a family member may be an owner but not a part of the management team; another family member may be a part of the management team but not an owner of the business. As the involvement of each family member in the business varies, consider the compensation model that will ensure the success of the business as well as family members.

3) Tax considerations

Be mindful of the benefits of tax considerations as an integral component of your plan. Tax planning can not only help reduce taxes in your business succession, but can also allow you to retain control of your company during the transition period, while at the same time provide you with the flexibility to decide which family members will receive what share of the family business and when. These plans generally involve the implementation of an “estate freeze” and the use of a family trust.

An estate freeze can allow you to pass the future growth of the business to the next generation on a tax-effective basis while retaining control of your business—an important option. Using a discretionary family trust to own the new common shares in an estate freeze can help ensure flexibility in succession planning. Dynamics can change in a family.

It is advisable to plan ahead and start the succession process well in advance. The shares of the family business can represent a significant asset; therefore, careful planning is required to help ensure the value is maintained and increased throughout the succession process.

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