



**PLAN NOW...**  
**Directions are not enough!**



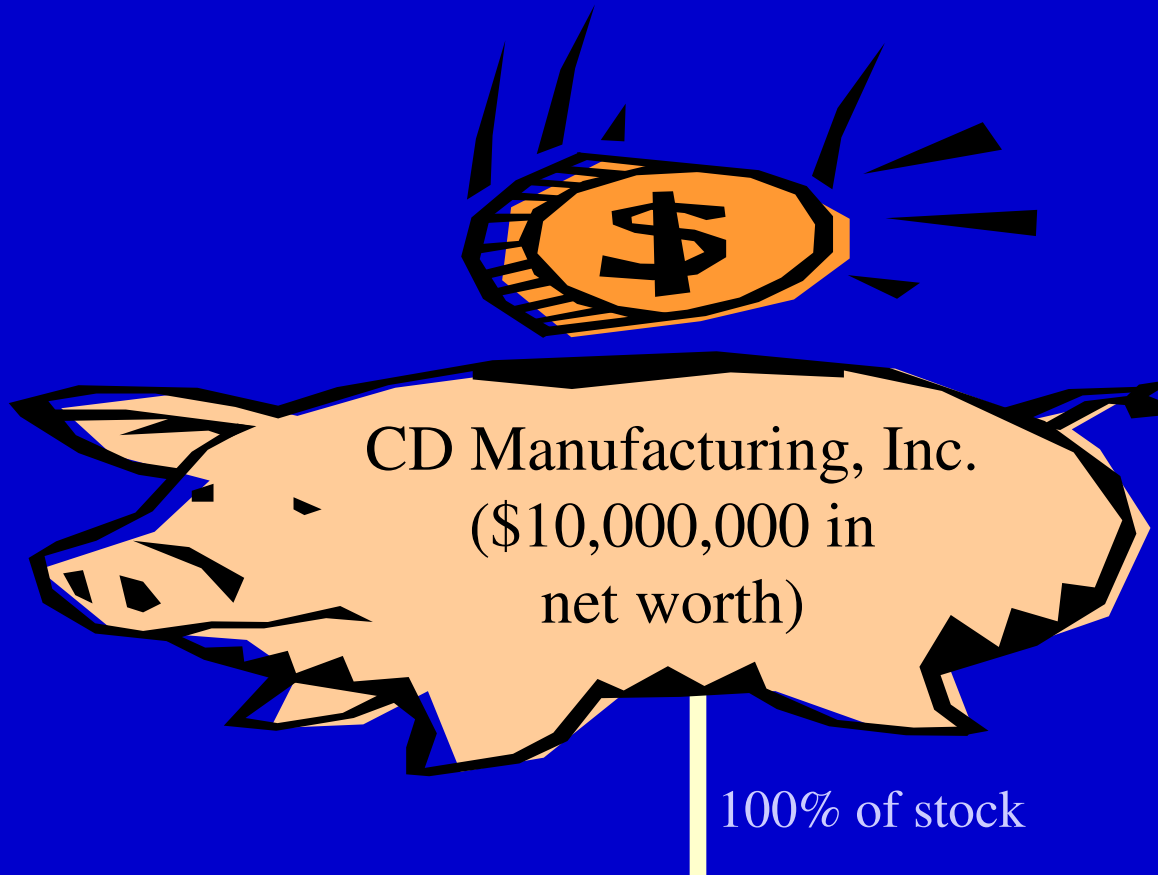
Founder of CD Manufacturing  
is heart attack victim

CD MANUFACTURING, INC. CLOSES  
WITH DEATH OF FOUNDER

LIQUIDATION SALE SAVINGS  
...all assets must be sold for taxes

# CD Manufacturing, Inc.

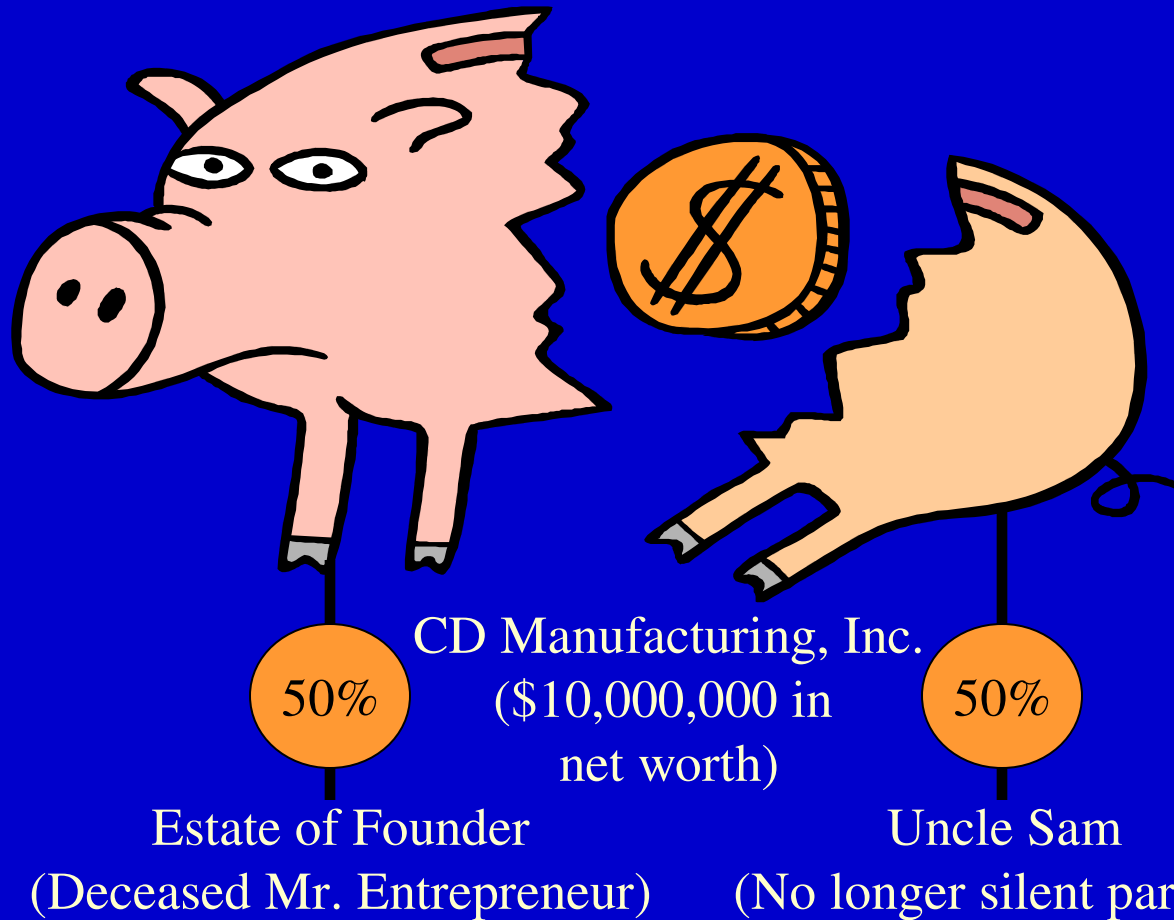
Before death of founder



100% of stock  
**EDDIE ENTREPRENEUR**

# CD Manufacturing, Inc.

After death of founder  
(An ownership illusion shattered)

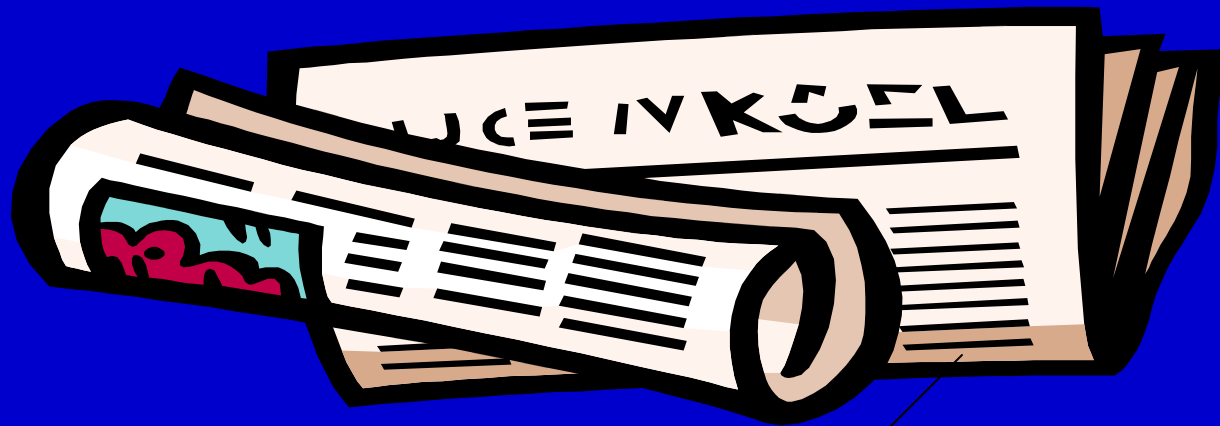




Prominent Business Owner Dies  
In Air Crash

Family factions file suit  
for control of Money, Inc.

**MONEY, INC. ANNOUNCES  
FURTHER LAYOFFS**



## Business Obituaries

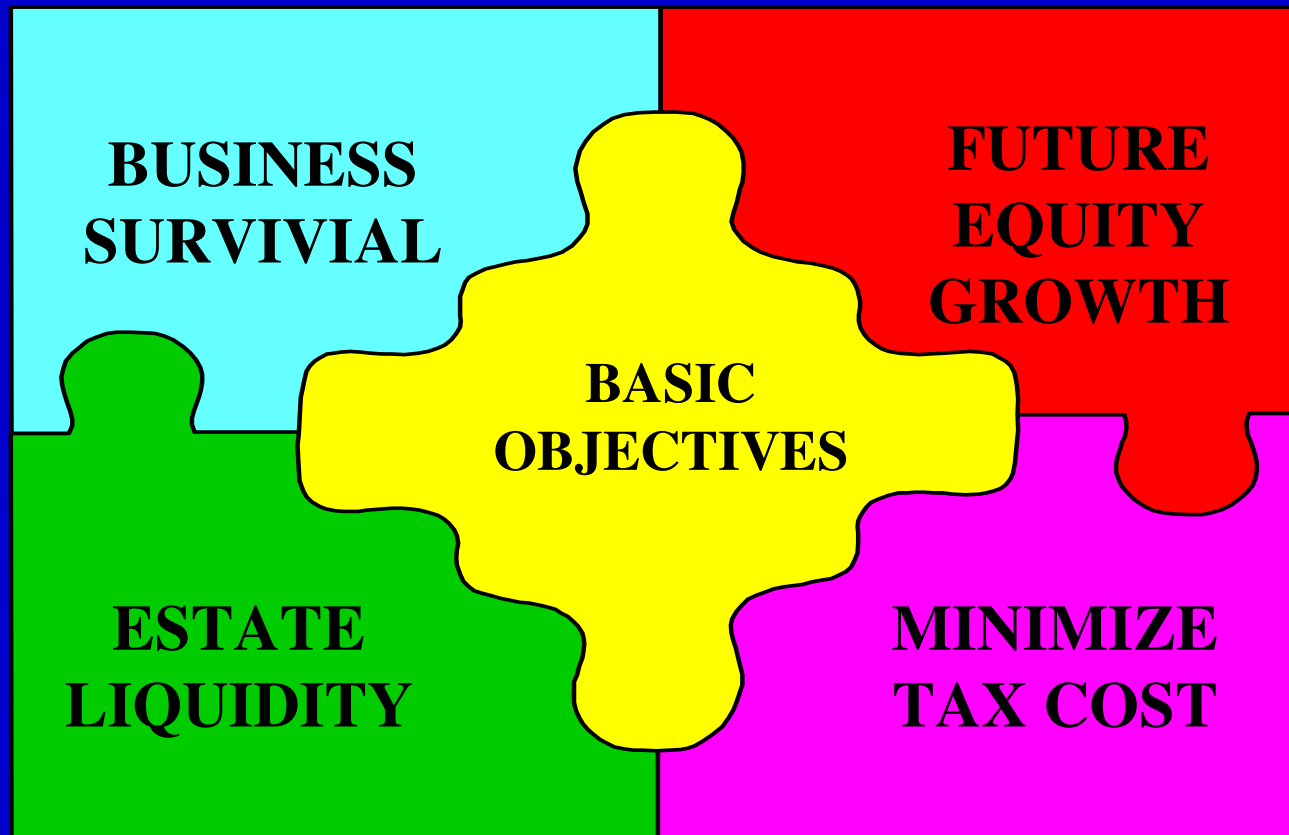
1. CD Manufacturing, Inc. - \$
2. Money, Inc. – People
3. What awaits you?

# Business Succession Planning

Planning for the transfer of  
Present Ownership and Management  
of the closely held business  
to others



# The basic objectives of succession planning...





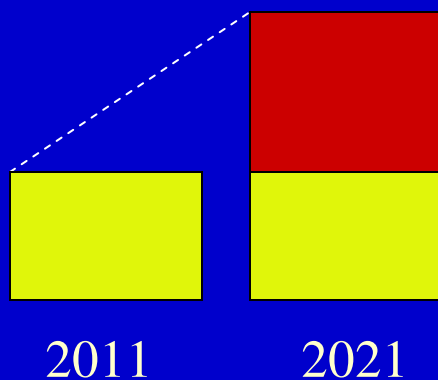
# What is Future Equity Growth?

Asset Increasing  
at 8% Growth Rate

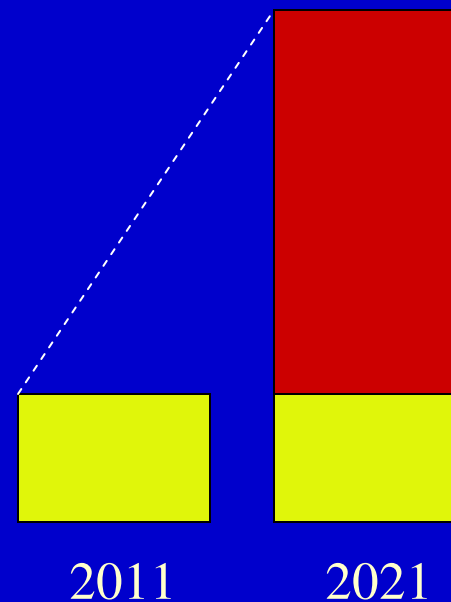
\$4.41 Million

2.16 Million

1 Million



Asset Increasing  
at 16% Growth Rate





# Business Growth and Estate Taxes

*Exemption:  
Max Tax Rate*

	2011-12	2013+
Exemption	5,000,000	1,000,000
Max Tax Rate	35%	55%

VALUE	2011-12	2013+
20,000,000	12,500,000	13,780,000
10,000,000	2,500,000	4,780,000
5,000,000	0	2,030,000
3,500,000	0	1,205,000
2,000,000	0	435,000
1,500,000	0	210,000
1,000,000	0	0

Average p/e multiple for S&P company: 20.18 (As of Sep 2011)

S&P Ten year p/e range: 15 to 36 (2001 to 2011)



# Business Growth and Estate Taxes

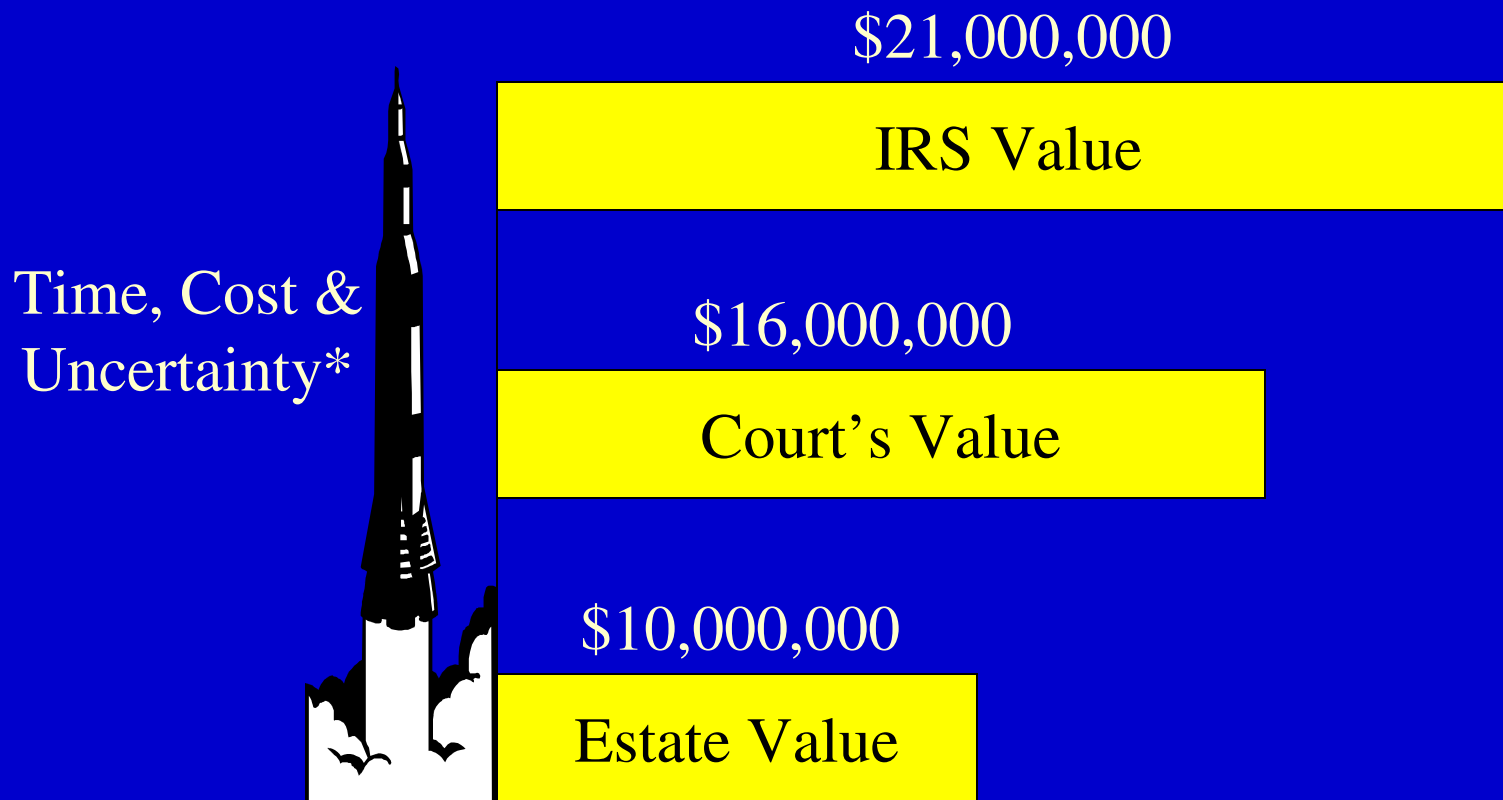
	2007-08	2009	2010
<i>Exemption:</i>	2,000,000	3,500,000	
<i>Tax Rate:</i>	45%	45%	0
<b>20,000,000</b>	<b>8,100,000</b>	<b>7,425,000</b>	<b>0</b>
<b>10,000,000</b>	<b>3,600,000</b>	<b>2,925,000</b>	<b>0</b>
<b>5,000,000</b>	<b>1,350,000</b>	<b>675,000</b>	<b>0</b>
<b>3,500,000</b>	<b>675,000</b>	<b>0</b>	<b>0</b>
<b>2,000,000</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>1,500,000</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>1,000,000</b>	<b>0</b>	<b>0</b>	<b>0</b>

**VALUE**

Average p/e multiple for S&P company: 24.9 (As of 12/04)

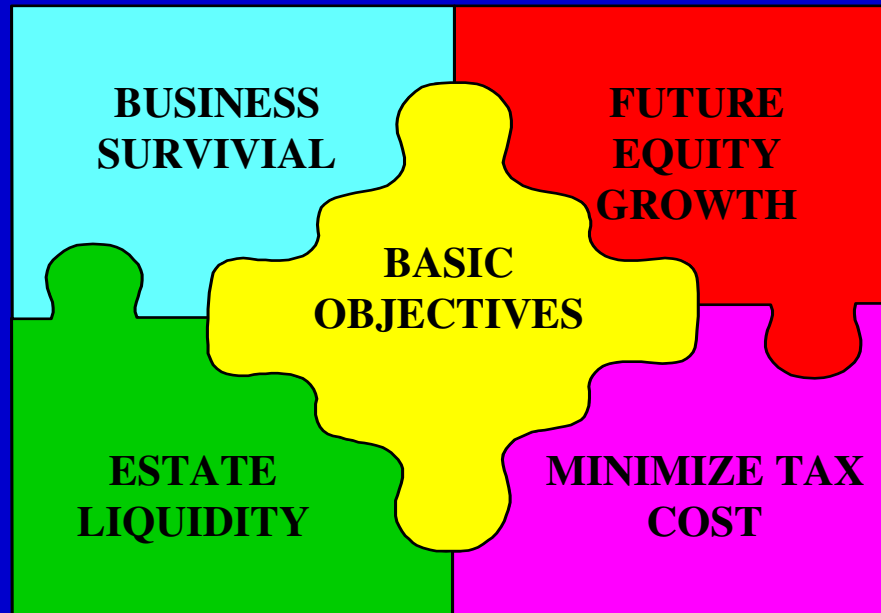
S&P Ten year p/e range: 17 to 46 (1994 to 2004)

# Survey of Court Valuation Cases

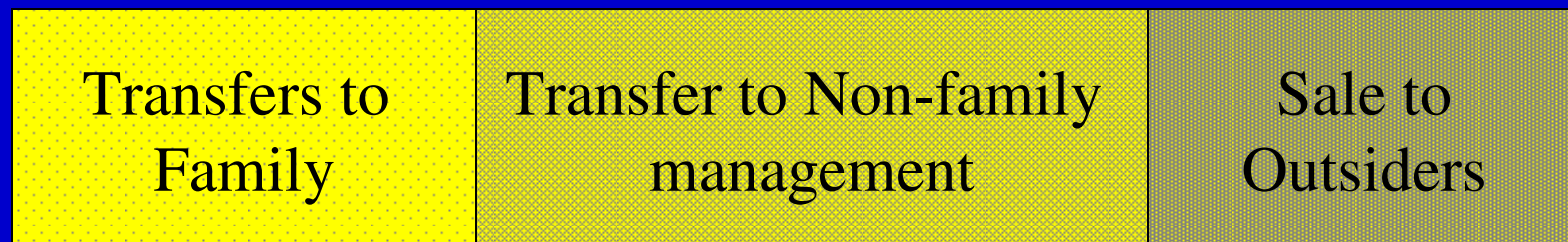


\*TIME AVERAGES 5 YEARS, 10 MONTHS FROM DATE OF DEATH TO COURT DECISION

# The basic objectives of succession planning...

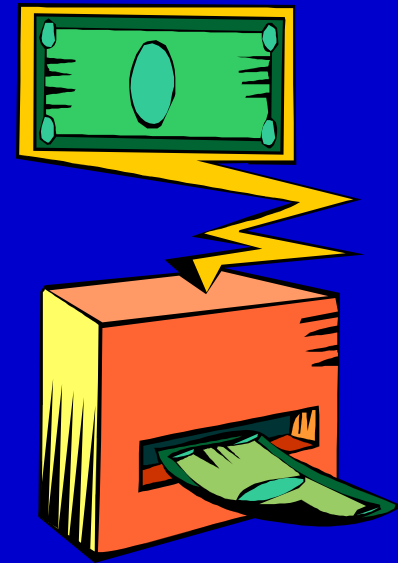


## Succession Decision Making Techniques...



# Transfers to Family

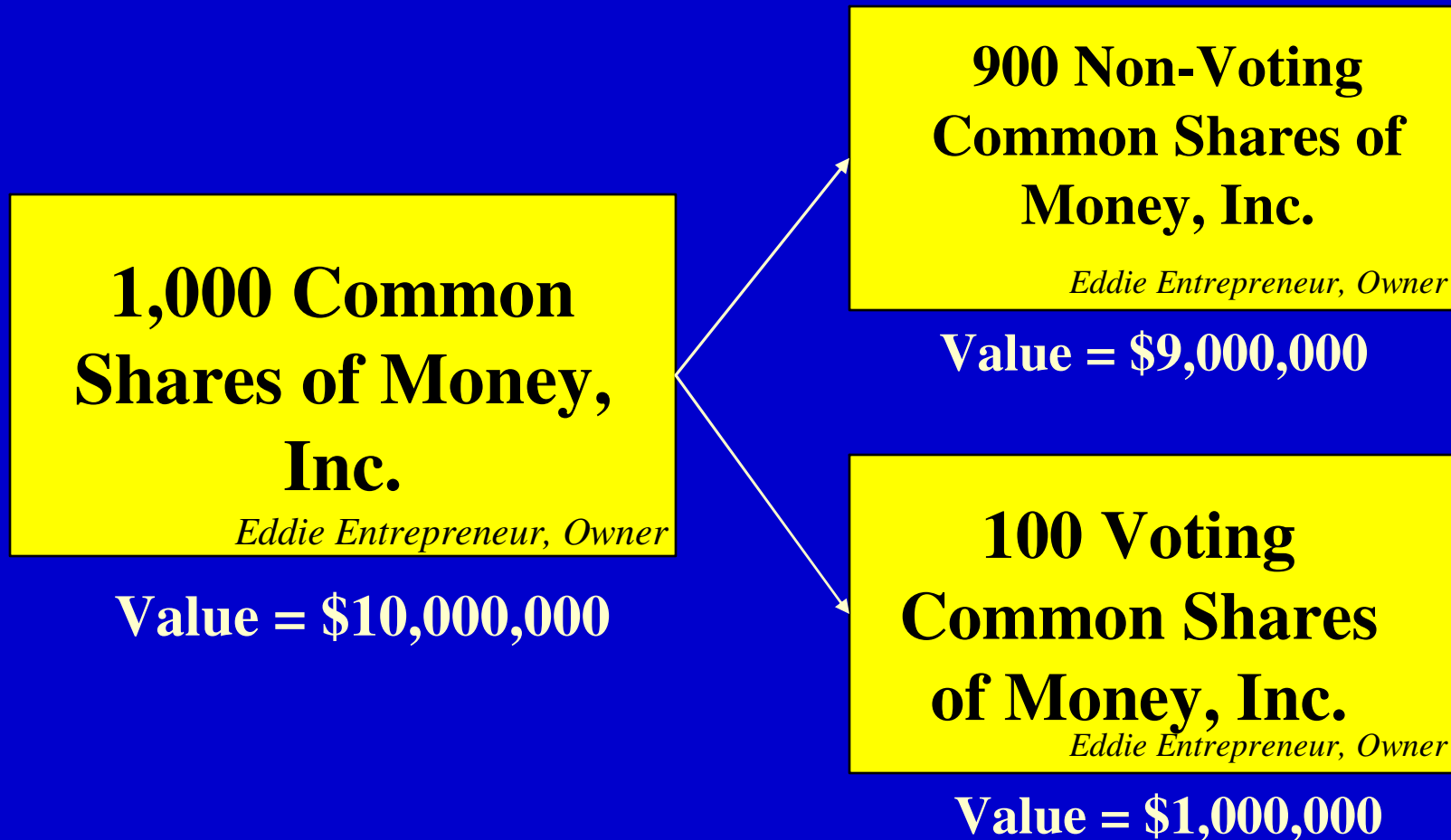
- Voting/Non-Voting  
Stock Recapitalization
- Gift/Estate Plan
- Buy-Sell Agreement
- “Growth” Subsidiary
- Sidewise Sale
- Sales – Installment or Lump Sum



# Set Family Goals and Economic Objectives

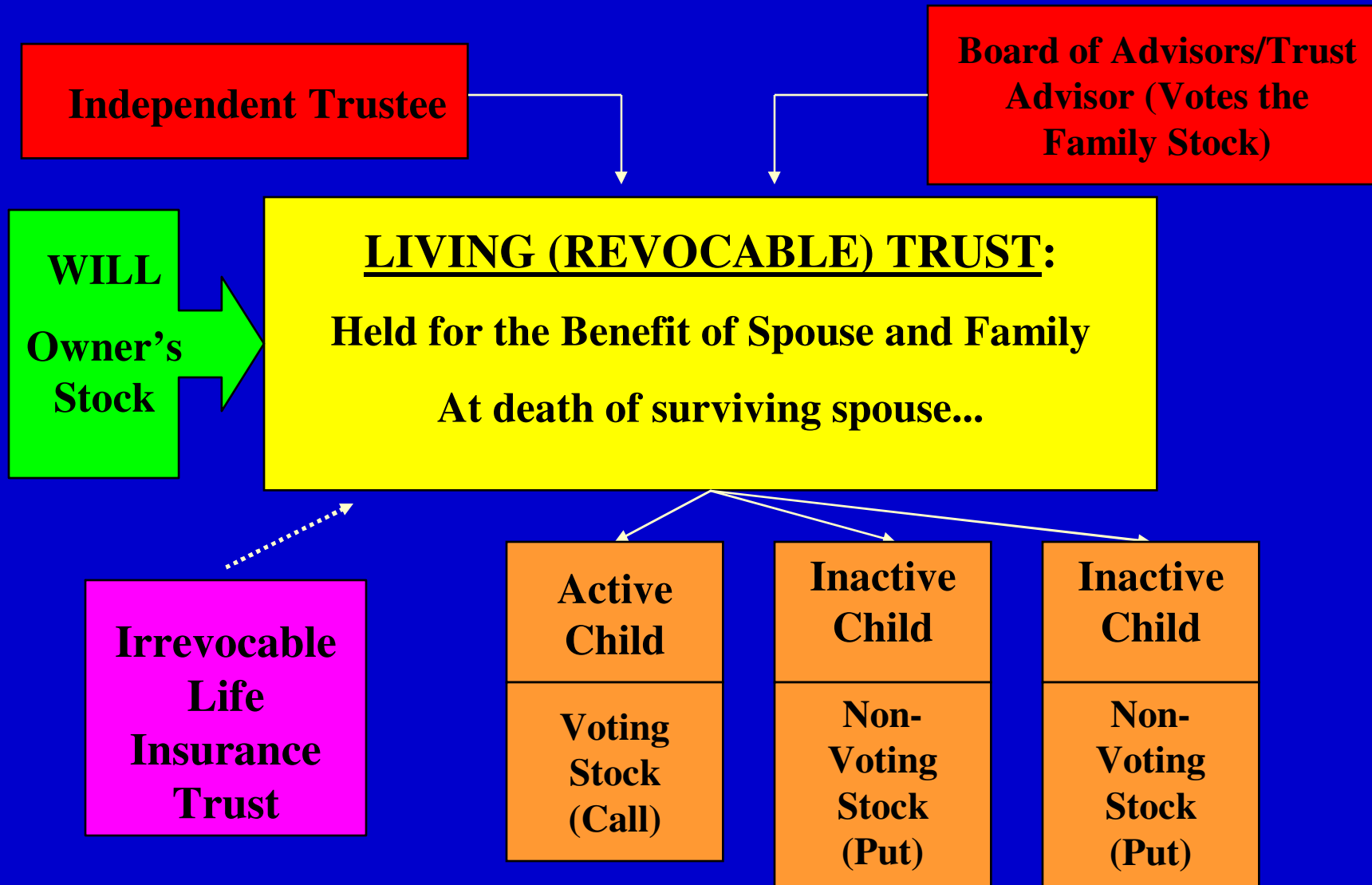


# Common Stock Recapitalization





# Gift Estate Plan



# Gift Estate Plan

## ADDITIONAL DOCUMENTS

1. Power of Attorney for Financial Matters
2. Health Care Power of Attorney
3. Living Will

# Why Make Gifts Today?

## A. *GIFT AND ESTATE TAX RATES*

*SAME AND CUMULATIVE*

## B. *PAYING GIFT TAX REPRESENTS*

*PREPAYMENT OF ESTATE TAX*

## C. *WHY CONSIDER?*

- Certain gifts tax-free
  - \$13,000 annual exclusion per person
  - \$5,000,000 lifetime exemption (thru 2012)
  - \$1,000,000 lifetime exemption (after 2012)
- Shift Control
- Shift future appreciation
- Ease liquidity demands at death
- Personal reasons
- Shift future income tax



# Set Family Goals and Economic Objectives



# Buy-Sell Agreement (Mandatory Sale at Death)

- Corporate Redemption
  - Business Insurance
- Shareholder Purchase
  - Cross Purchase Insurance  
(Each shareholder insures the other's life)
- Lump Sum or Installment Buy-Out



# Buy-Sell Agreement (Mandatory Sale at Death)

- Other Key Provisions
  - Right of First Refusal
  - Options to Buy/Sell in event of Disability or Retirement
  - Valuation Formula
  - GAAP Accounting Issue



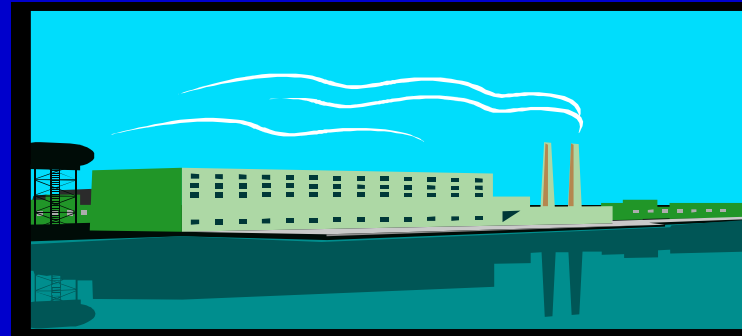
# The “Growth” Subsidiary (LLC)



Children  
and/or “in-laws”  
30%



Mom and  
Pop  
70%



Existing Company

# The “Growth” Subsidiary (LLC)

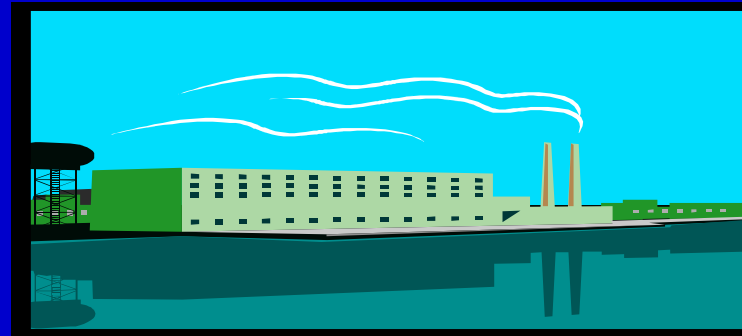


Children  
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30%



Mom and  
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70%

100% COMMON  
STOCK FOR  
\$100,000



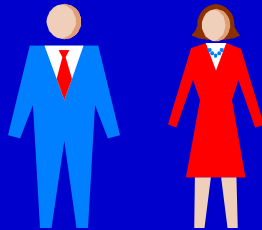
Existing Company



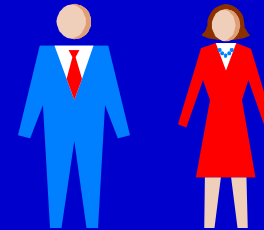
“Growth” Subsidiary  
Or LLC



# The “Growth” Subsidiary (LLC)

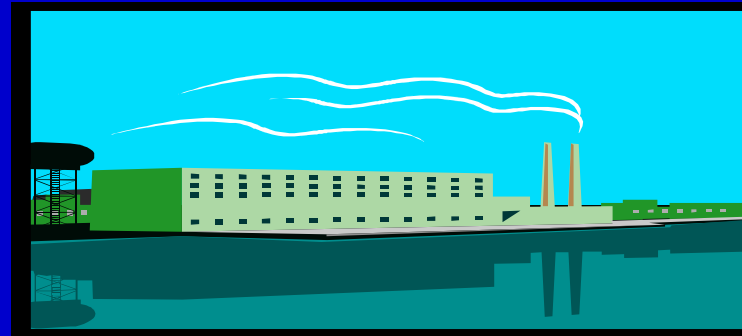


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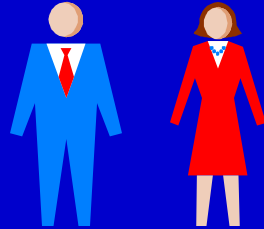
Existing Company

\$1,000,000  
PREFERRED  
STOCK

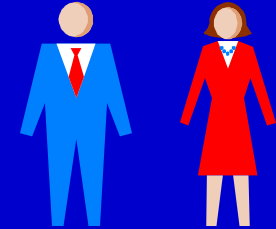


“Growth” Subsidiary  
/LLC

# The “Growth” Subsidiary (LLC)

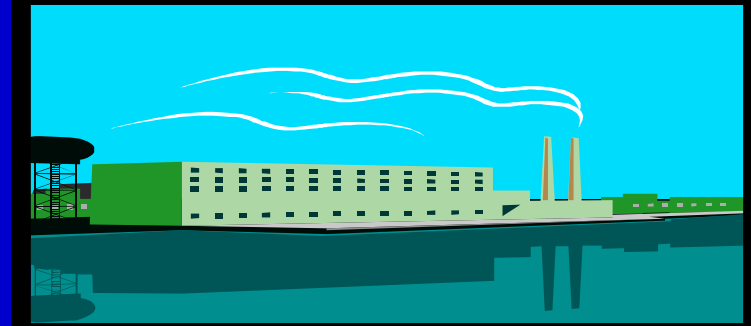


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Mom and  
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70%

100% COMMON  
STOCK FOR  
\$100,000



Existing Company

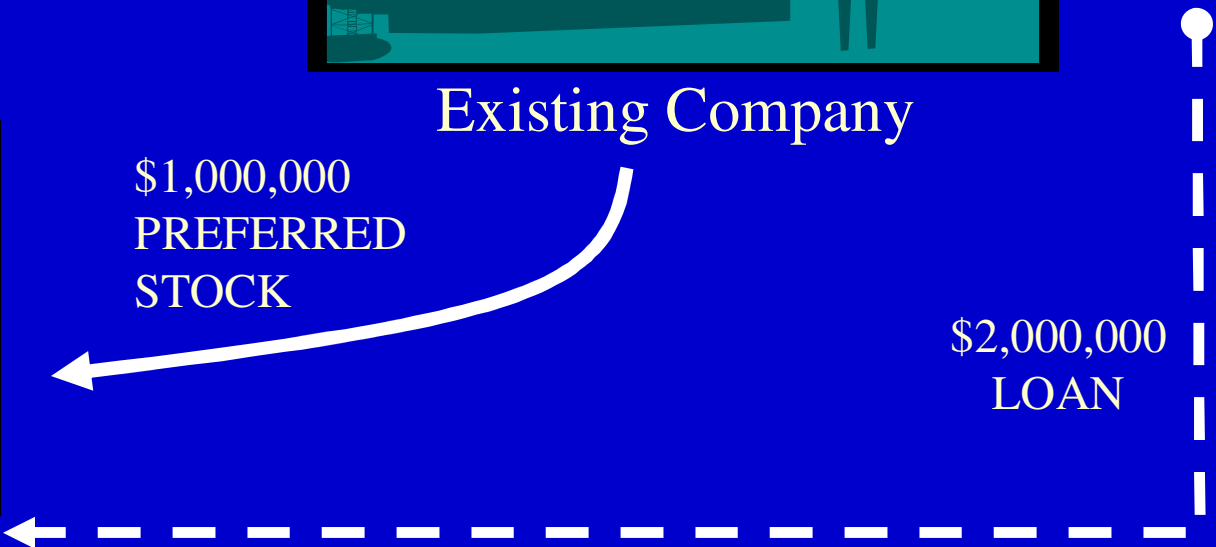


“Growth” Subsidiary  
/LLC

\$1,000,000  
PREFERRED  
STOCK



\$2,000,000  
LOAN



# Sidewise Sale

FOUNDER AND  
INACTIVES

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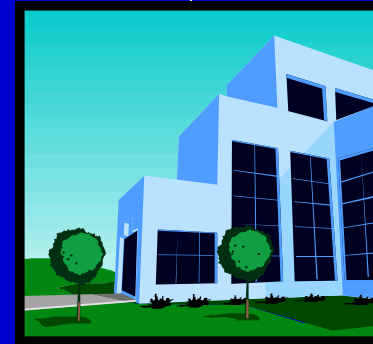


**OLD COMPANY**

Convert to Family Leasing  
and Investment Company

ACTIVES  
(SUCCESSOR GENERATION)

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**NEW COMPANY**

Successor Operating  
Company

# Sidewise Sale

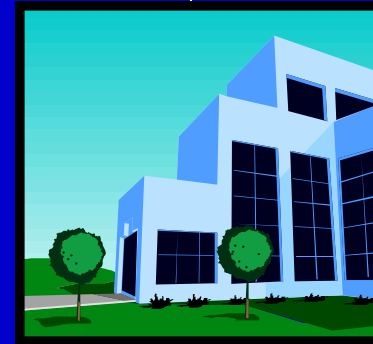
FOUNDER AND  
INACTIVES



OLD COMPANY

Convert to Family Leasing  
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ACTIVES  
(SUCCESSOR GENERATION)



NEW COMPANY

Successor Operating  
Company

(1) Sale of Operating Assets

# Sidewise Sale

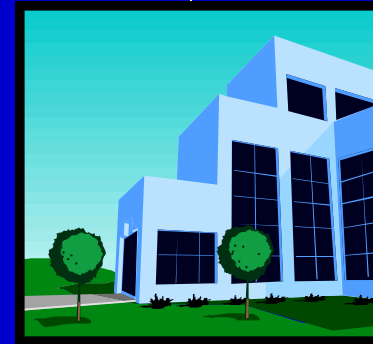
FOUNDER AND  
INACTIVES



OLD COMPANY

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ACTIVES  
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NEW COMPANY

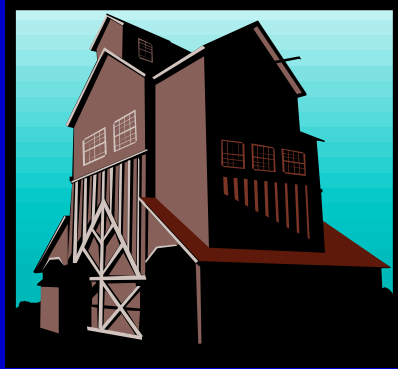
Successor Operating  
Company

(1) Sale of Operating Assets

(2) Lease Fixed Assets

# Sidewise Sale

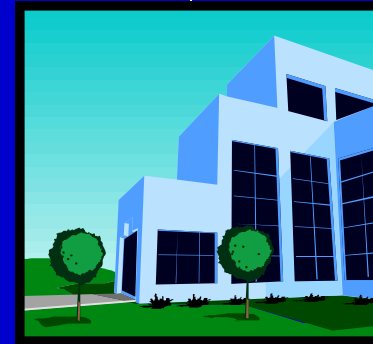
FOUNDER AND  
INACTIVES



OLD COMPANY

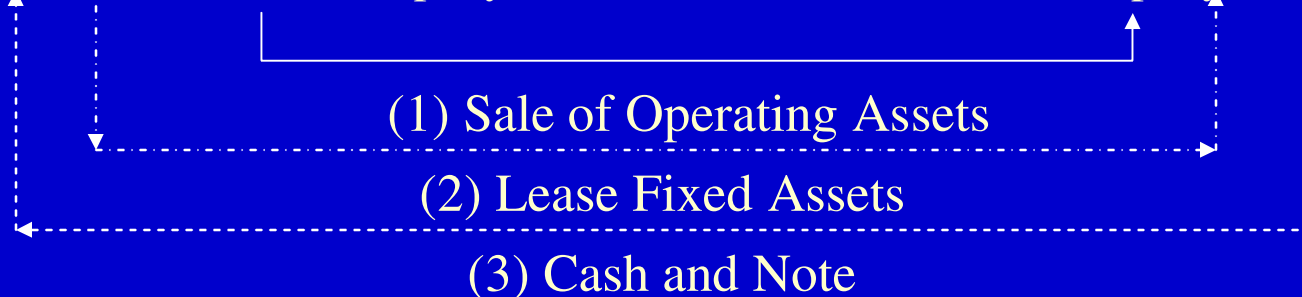
Convert to Family Leasing  
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ACTIVES  
(SUCCESSOR GENERATION)

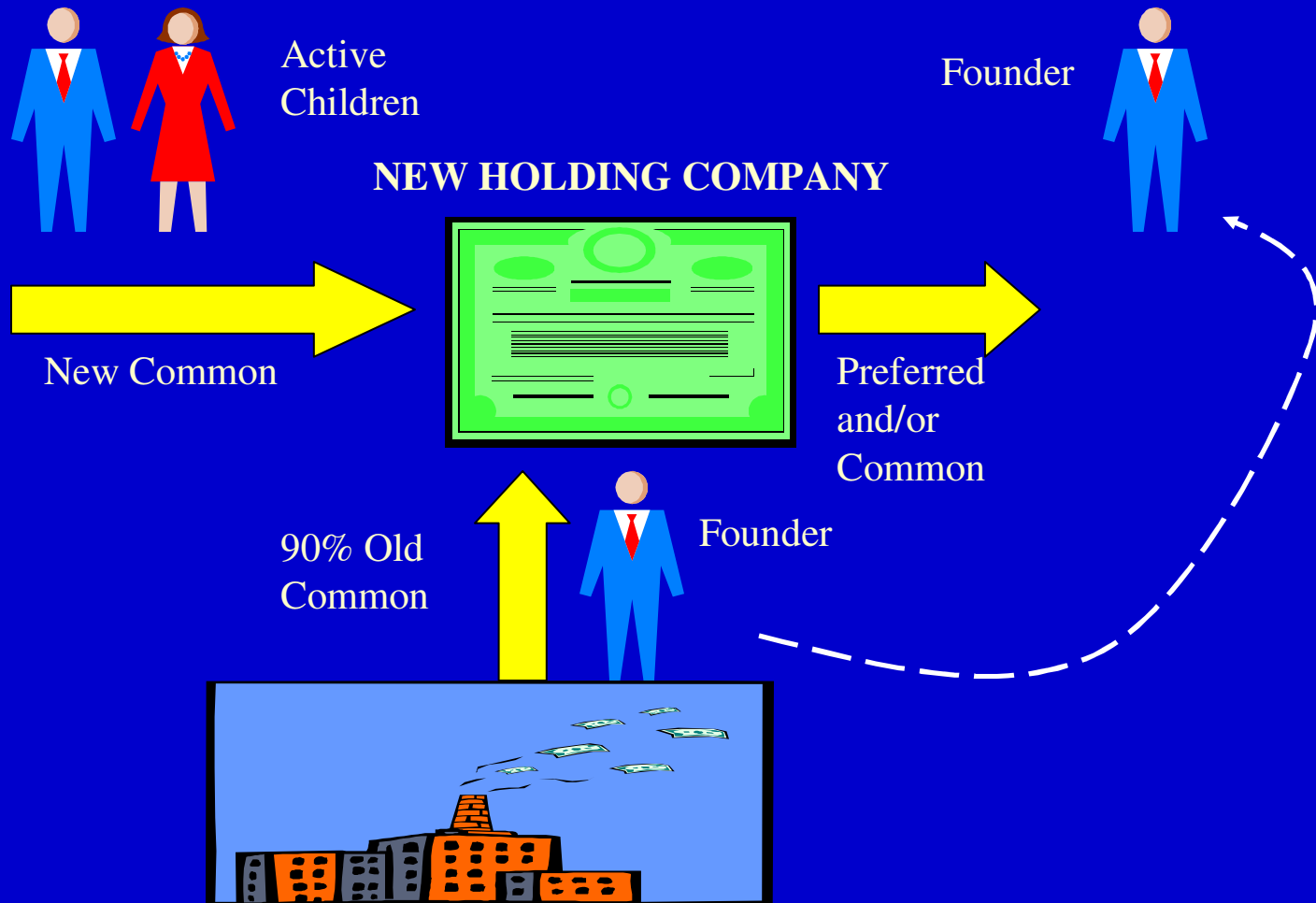


NEW COMPANY

Successor Operating  
Company



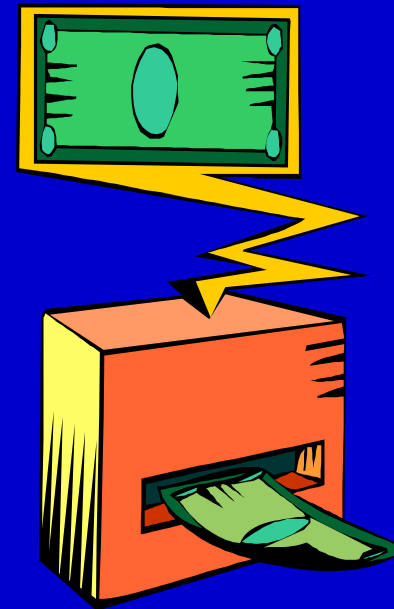
# Holding Company (Subsidiary Conversion)



**OPERATING COMPANY**

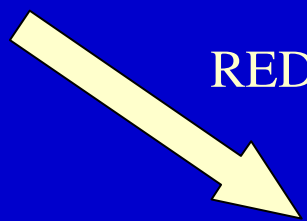
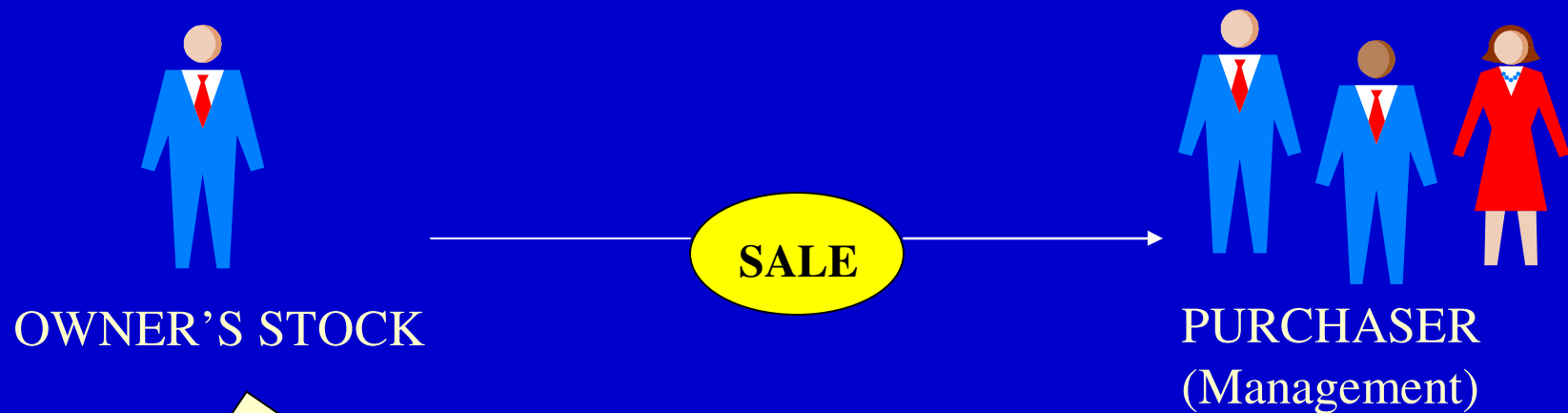
# Transfer to Non-Family Management

- Bootstrap Sale (Stock)
- Installment Sale (Assets)

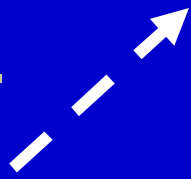




# BOOTSTRAP SALE



REDEMPTION



**CORPORATION**  
• Cash  
• Borrowing Ability

- LUMP SUM
- INSTALLMENT SALE

Caveat: Debt or Equity

# Sale of Business

## COMPARISON: Sale of Stock vs. Sale of Assets

Owner:

<u>SALE OF STOCK</u>	\$5,000,000
Stock basis	- <u>100,000</u>
Taxable gain	\$4,900,000

### CORPORATION

<u>SALE OF ASSETS</u>	\$5,000,000
Asset basis	- <u>4,500,000</u>
Taxable gain	\$ 500,000

# STEPPED-UP BASIS CONCEPT

## A) PRE-DEATH INCOME TAX COST

Owner's appreciated assets –  
taxes on pre-death sale:

Fair market value	\$5,000,000
Owner's basis (cost)	<u>100,000</u>
Approximate Taxable Gain	\$4,900,000

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## B) POST-DEATH SALE

Fair market value	\$5,000,000
Stepped-up basis	<u>-5,000,000</u>
Taxable Gain	-0-

# LIQUIDITY FOR DEATH COSTS

## A. OTHER ASSETS

- Liquid assets and borrowing
- Insurance advantage

## B. SECTION 303 REDEMPTION PLAN

## C. BORROW FROM U.S. – SECTION 6166

## D. BUILD EARNINGS OUTSIDE COMPANY

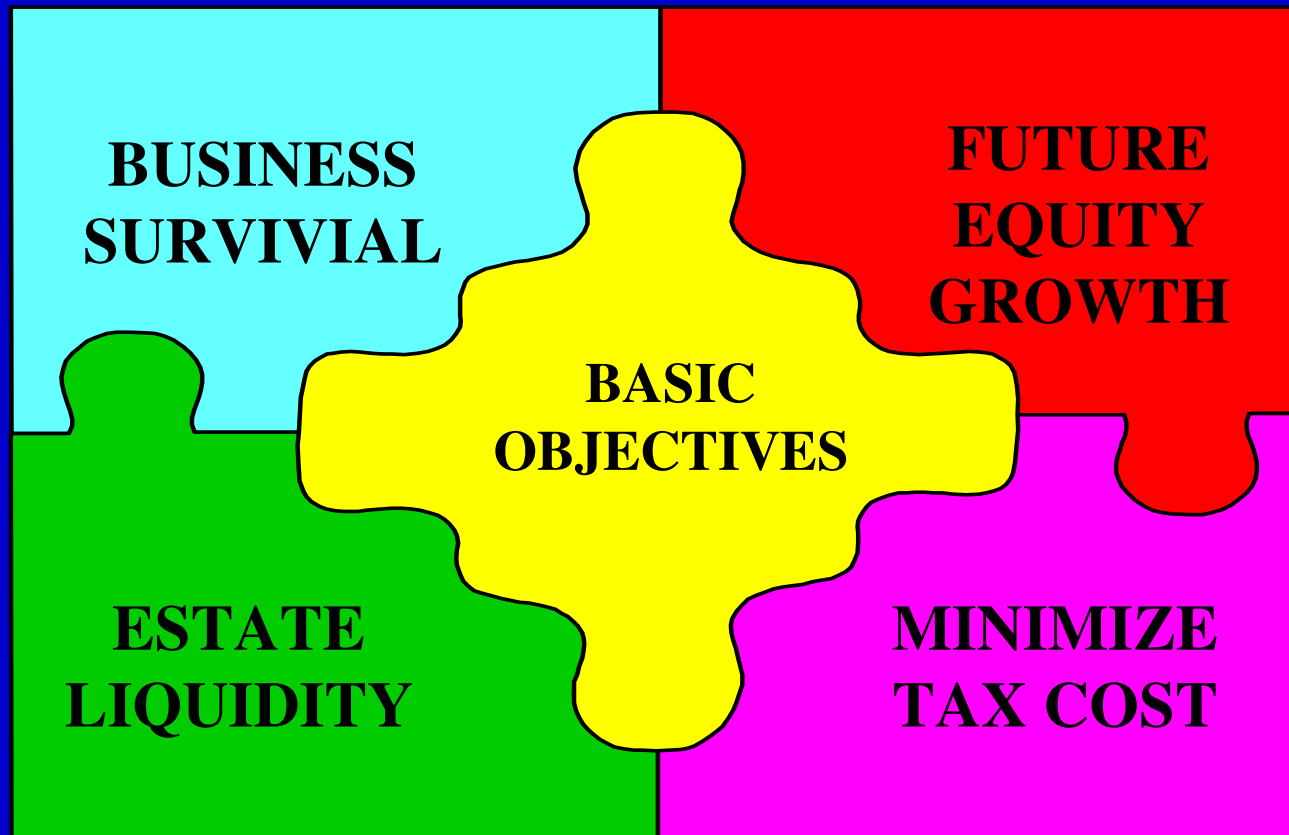
## E. LEVERAGE



# SUCESSION PLANNING CASE STUDIES



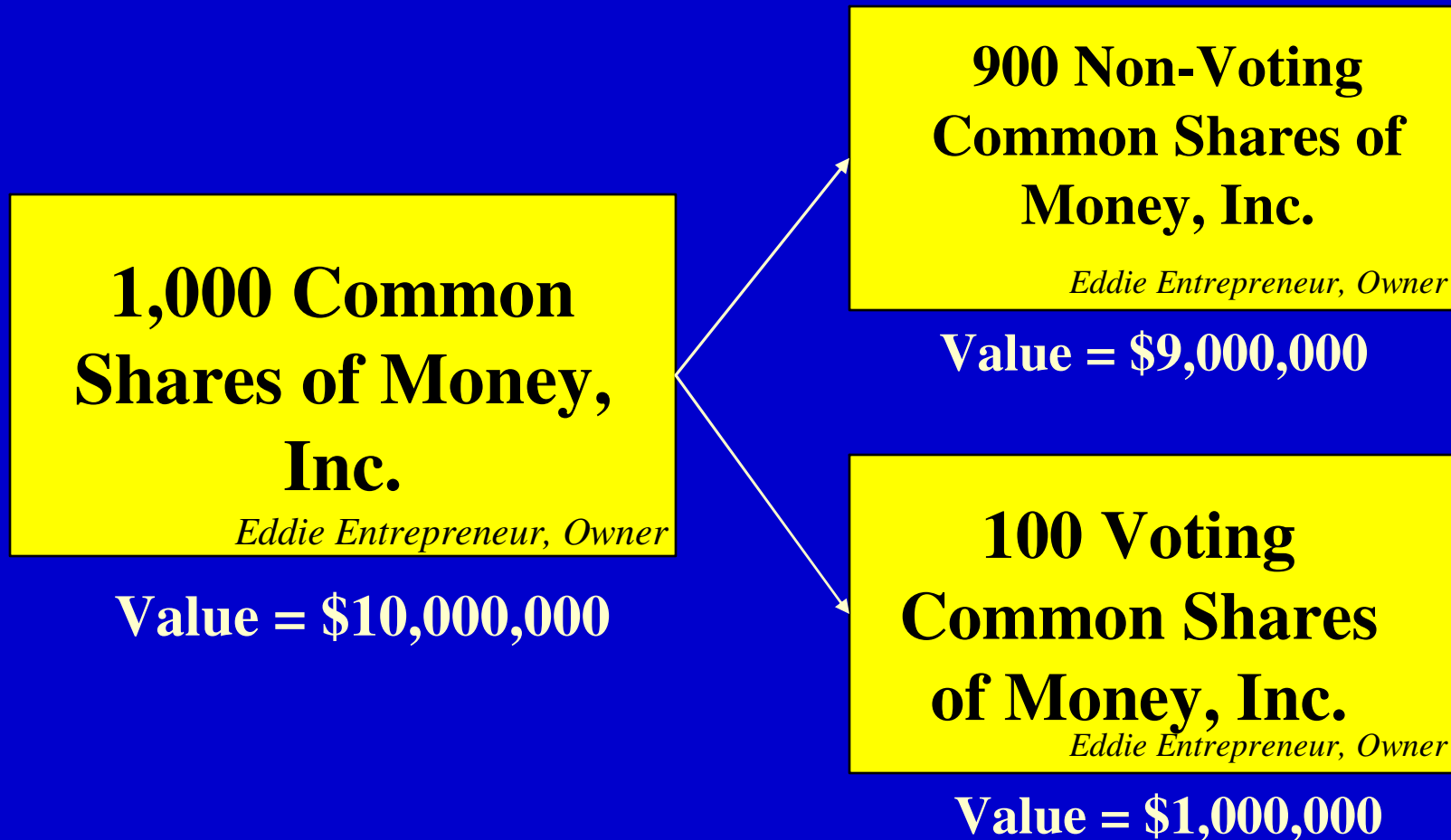
# The basic objectives of succession planning...



## Case Study #1: CD Manufacturing, Inc.

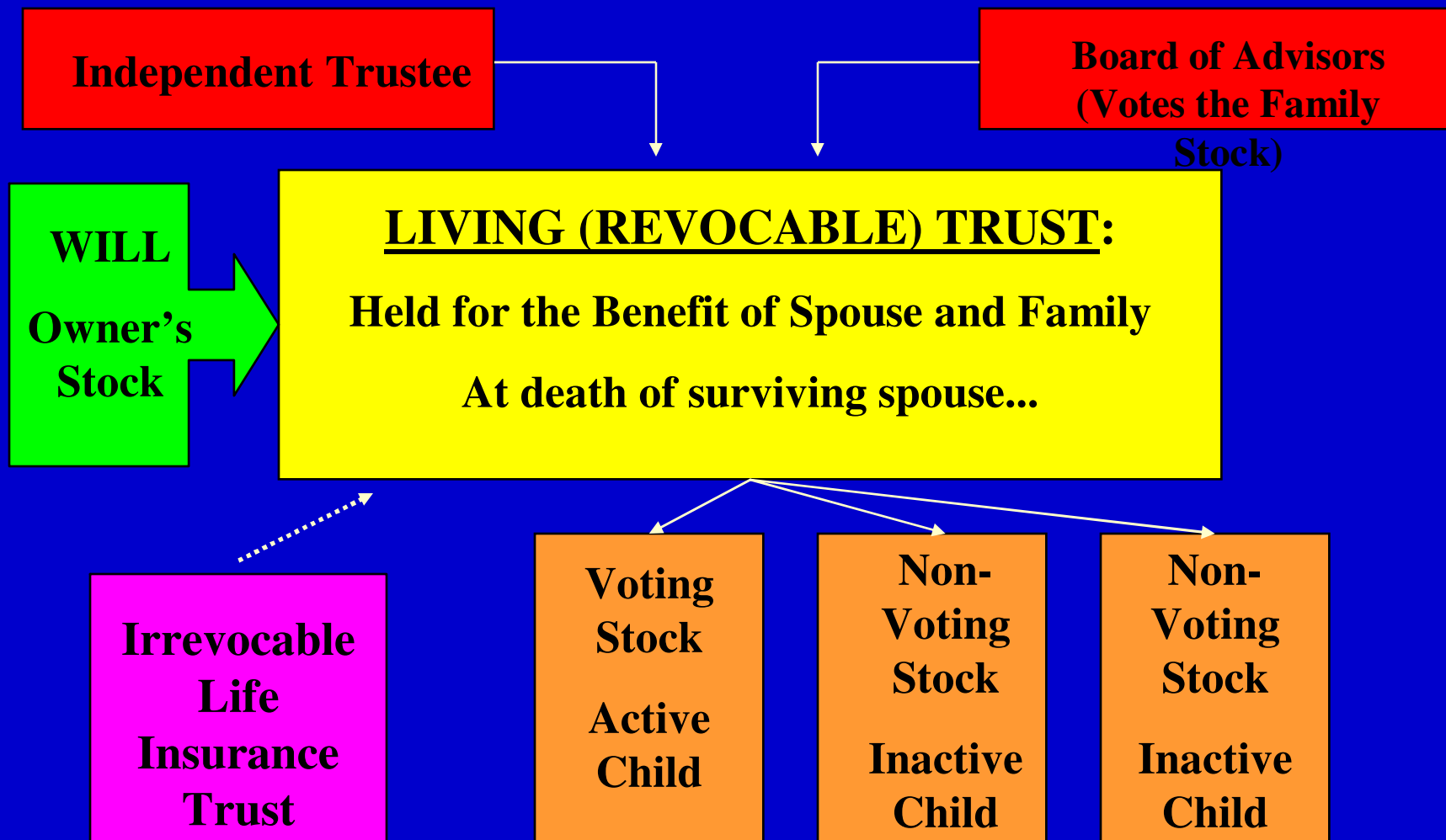
- Sales of \$50,000,000; Value \$10,000,000
- Lots of Assets
- No Long Term Debt, but uses A/R Facility
- 100% Owner, Age 60
- 4 Children, 2 Inside, 2 Outside
- 401(k) = \$1,000,000
- Personal Assets = \$3,000,000
- \$3,000,000 Life Insurance

# Common Stock Recapitalization





# Gift Estate Plan



# Case Study #1 Solution

- Common stock recapitalization
  - 90% nonvoting / 10% voting
- Gift estate plan
  - Voting stock divided among active children
  - Nonvoting stock divided among inactive children
    - Stock “put” at predetermined formula price or appraisal
    - Life insurance funding
  - Annual gifting program and unified credit
- Deferred compensation for senior family members

## Case Study #2: Money, Inc.

- **Sales \$10,000,000; value \$2,000,000**
- **Inventory, few other assets**
- **Bank debt = \$1,000,000 credit line; \$500,000 term loan**
- **Ownership is 50/50 between one brother (age 55) and one sister (age 65)**
- **B has 3 children, one is 25 and works in operations; S has 2 children, one is 35 and is the top sales person**
- **401(k): \$400,000 each**
- **Personal assets: B = \$500,000; S = \$1,000,000**
- **Life insurance: B = \$1,000,000; S = \$50,000 (uninsurable)**

# Mandatory Sale at Death

- Corporate Redemption
  - Business Insurance
- Shareholder Purchase
  - Cross Purchase Insurance  
(Each shareholder insures the other's life)
- Lump Sum or Installment Buy-Out



# Case Study #2 Solution

- Buy-sell agreement
  - Death, disability, termination of employment
  - Life insurance funding to the extent available to B through an irrevocable trust (None for S)
  - % of cash flow for balance of payments
- Deferred compensation upon retirement
- Estate Plan: Living trust to utilize unified credits
- Powers of Attorney for financial and medical matters
- Establish advisory board to develop skills of next generation

# *Questions?*

*Frank P. Nagorney, Esq.*



*4600 Euclid Avenue, Suite 400*

*Cleveland, Ohio 44103*

*frank@cowdenlaw.com*

*Phone: (216)241-2880*

*Fax: (216)241-2881*