[Academic Script]

Succession Planning-2

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Unit No. & Title:	Unit – 5 Succession Planning
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Academic Script

1. Introduction

In the last session, you got an orientation to the concept and relevance of succession planning. Moving further with the topic, we shall now look into some specific process in succession planning, like estate planning. The session will also acquaint you to the importance of a career plan for the successor, how the successor's expectations and stress needs to be managed and how can the senior generation prepare the future generations to assume responsibility of the family business.

Objectives:

- To understand the process of Estate planning as a calculated measure pursued by the owner.
- To understand the expectations of the successor while designing the succession plan
- To understand the need for a sound career plan for the successor and opportunities for self-development
- To understand the relevance of building the future generation and the role played by the senior generation towards this end.

[E] Estate Planning:

When an outgoing older generation is planning their retirement, the preservation and eventual transfer of their family assets become a major concern. Estate planning aims to deal with the income taxation based consequences of such decisions. Owners are bound to hold properties amassed during their lifetime which they intend to pass on to their family members, post their death. These properties are bound to taxes, which are desired to be limited to their minimal.

Estate planning may appear as a complex task, but if it is treated as a well planned exercise then it can really benefit the successive generations. The key concerns regarding an estate plan are as follows:

- Expert Assistance

  Estate plans must be developed with due assistance of attorneys or tax advisors. They can assist the concerned in developing the fundamental documents and processes. Generally the documents include a declared will, power of attorney or a health care proxy and other tax related processes. They can assist with making decisions by considering the implications of each of the considered options. Their expertise can assist the concerned in correctly articulating their wishes, minimizing taxes and incorporating changes with changing circumstances.

- Maximizing the gains

  The core idea of estate planning is to maximize what the owner leaves for the family members, the spouse or the heir apparent. Thereby it is very important to get legal and tax guidance regarding how each asset will pass to the beneficiaries. The choices are bound to vary by the asset type, asset size, the age of the owner, and such other factors. The idea is to design it in a fashion that little is lost to taxations, court fees and other related expenditures.

- Estate, inheritance, and gift taxes

  Tax minimization is the core objective in estate planning. Taxes on gifts and estates can be among the highest assessed on any financial transaction. This can be further charged with state based levies on estate or inheritances. These taxes usually have exemption limits, which is used by many people to transfer assets while they are still living to ensure maximized inheritance for their beneficiaries. Such Estate and inheritance taxes usually are based on the valuation of the estate and are paid before the assets are distributed to the beneficiaries.

Estate Planning covers these concerns by doing appropriate planning during the lifetime of the owner, and includes taking any of these measures:

- financial planning;
- estate freeze;
- life insurance;
- asset transfer
- shareholders' agreement, if any;
- powers of attorney in the event of incapacity;
- planned charitable giving, and
- will planning.

Estate freeze/refreeze

An estate freeze is an approach towards limiting death taxes. It entails transferring he growth potential of assets such as real estate or shares of corporations to the younger generation. The asset value to the transferor is frozen at its value as on the date of transfer. It also leads to freezing the amount of potential capital gain.This allows in estimating the potential tax liability on death and hence equip the firm with plans for the payment of income taxes. An estate transfer is usually accomplished through a transfer of assets to a corporation or an internal capital restructuring. The transfer ought to be professionally planned though. There is also an option of refreezing the previously frozen assets at the lower current value, and the future increase in value can benefit the other (generally younger) family members.

Life Insurance

Life insurance is a very frequently employed estate planning too. If the estate is high on liquid assets, then that supports tax payments. On the contrary if the estate consists of shares of private companies or real estate then it may lead to difficulties in settlement without selling off the assets.

Life insurance can be an effective estate-planning tool to fund future tax requirements. Policies that are properly structured can yield enough insurance proceeds that can fund adequately the tax amounts at time of the death. However since insurance needs can be constantly evolving, reviewing coverage on a regular basis is of utmost importance.

Asset Transfer

In the event of possession of excessive assets and if the owner wishes considering reducing estate probate and executor fees, and also possibly income taxes upon death, then the owner can transfer assets during their lifetime. However the owner needs to carefully assess which assets to transfer, to whom, and how to avoid attracting a tax liability.

Planned giving

Other way of minimizing income taxes and estate administration fees is by making charitable donations during the owner's lifetime. The income tax credits during the life of the owner are an added benefit. In addition to that it also leads to the reduction of probate fees and other estate costs. Planned giving may assume many forms. It can involve gifts of life insurance or setting up of private foundations or trusts.

Such a measure requires sound advices from tax advisors to design a planned-giving strategy that is most appropriate to the owner's individual situation. There needs to be an appropriate look into estate planning, financial planning and tax planning to arrive at a sound planned-giving plan.

Will Planning

One of the most critical elements of an estate-planning strategy is the Will Planning. This should be treated with an inevitable disposition since a dying intestate (without a will) can nullify all the painstakingly pursued estate-planning provisions. If a owner dies without a will, then the assets stand distributed in accordance with the laws of the province where the owner resided. This may not necessarily be in accordance with what the owner would have wanted.

A will can only assure that the assets are duly distributed to the heirs and ensure that the wishes of the owner is upheld and respected. A Will can also help minimize taxation to the owner's beneficiaries by way of specific tax provisions like testamentary trusts and such specific modalities. However, the will needs to be reviewed periodically so as to incorporate changes happening at the personal family relationship dynamics.

2. Reviewing Estate Plan

Estate plans must be visited with revisions at regular interval.
It is very important that the owner updates the estate plan at regular intervals or during the course of key life events.
Generally owners review their estate plan at a regular frequency, often during review of their financial plans, and it can be done annually, semi-annually, or quarterly. The general recommendation with respect to estate planning is that they be revisited at least every three to five years or when there is a life event.

The Estate plan must be subjected to revisions during life events like the following:

- The birth or adoption of a new member; when a child in the family grows into an adult; when provisions are required for educational funding.
- In event of death of any member;
- Marriage or divorce; illness or any major disabilities caused;
- Change in your life or long-term care insurance coverage
- Procuring huge borrowings or purchase of major assets;
- Changes in laws pertaining to taxes and investments

3. Expectations of Successors

Young family successors in any family business usually find themselves in a unique situation. It can be complex and stressful. Stress is a resultant of being in conflicting roles and the constant need of coping with mixed expectations.

How do the Successors cope with the stress?

A healthy successors accepts and acknowledges the inherent issues of being a successor, thereby resorts to proactive steps to handle the stress. Few such efforts are discussed:

Building a perspective with reflection: Several successors recommend journal writing to be a valuable way to record valuable learning and to build confidence.. Many of them resort to self-help books to get a perspective.

Seeking allies from outside the business: Many successors join clubs, organizations or even informal groups of presidents or top representatives of family businesses. Some join university based entrepreneurs groups and bodies that help them look at other entrepreneurs sharing stories and encounters that they can relate to. It is in such situations that companies bank on the directors from outside the family to play the role of a mentor to the successor.

Act: Many times successors believe in just doing it out, rather than worrying about the consequences. Many successors have attempted courageous moves, taking genuine feedback to their strides and thereby making a mark for themselves in the eyes of the family and top management.

4. Self-Development and Career Plan

It is imperative for the next generation to see a future in joining the family business and to see it contributing their development of the self. The orientation to the family led business is not a day's job, it obviously extends to feeding positive thoughts about joining the business from the early years of the next generation. However, if it appears as forced and as the only option, then the children are bound to view it more of an obligation, and less of a perceived opportunity. And not showcasing it as an opportunity stands a danger of not building a sound positive mind towards business as a career opportunity. Thus swaying between the two extremes in a very calculated and planned way is the only resort to the parents in such family firms.

It calls for the next generation to weigh their choices well and to make necessary decisions pertaining to their self-development and career based on the following questions:

- What are the reasons that lead to the decision of joining the family business?
- Does the business fulfill the career aspirations?
- Will it be possible to fulfill the expectations of the senior generation?
- Would be there enough freedom and discretion to act independently or will it be like shadow living with the seniors?
- How easy or difficult would it be to work with siblings and cousins in the same organizational setup?
- Would it be easy to gain respect from the employees?

The Successors must always be allowed to access outside-the-firm experience. They should have access to building careers for themselves in forms outside of the family business clan. It will definitely help them to build their self-esteem and confidence to face real life business problems and to equip themselves with adequate problem solving approaches and mechanisms. It offers them a wider experience of the business operations. It also offers them an opportunity to build credibility among non-family team. This will contribute positively in establishing their values, beliefs and principles towards work.

5. Preparing the Next Generation

Family business owners must not give in to the temptations of favoring certain successors just because they appear similar in their views , conducts and aspirations. Succession process should never be viewed as cloning.

Following criteria must be considered while approaching a successor:

- Is the successor/s committed to the firm's mission?
- Does the successor/s has/have the ability to take the firm forward?
- Can they arrive at sound decisions?
- Do they have the leadership capabilities to lead and motivate others?

Often family businesses fall into the trap of a compulsory succession where the heir is forced to be a part of the business, where actually the heir desired an alternative career. In such cases, irrespective of the succession process, the results are going to be a utter failure. And in such situation it will make sense to get a management successor from outside, who will add far more value to the business then a forced family insider.

So only when the next generation shows the interest, should they be brought into the business and should be oriented to the ways of the business through a robust training.

Succession planning will accrue the desired results only when the older generation is involved in a well-planned partnership with the next generation and together, the following areas are duly considered:

- Ensuring that the children had always access to sound education.
- That they are morally nurtured with self-esteem and confidence.
- That they understand money matters in business and investments.
- That they are exposed to some good external work experience before joining the family business.
- And once they join they are offered an all encompassing training experience.

The family climate has a sound effect on the emotional and social intelligence level of the next generation. High degree of emotional and social intelligence fosters high degree of accountability and responsibility for their leadership behavior. Thus a positive family climate is an essential for a motivated, responsible and confident next-generation to take up the family legacy.

A family needs to practice open communication so as to create medium for the younger generations to share beliefs, values and aspirations. The senior generation must display high levels of interest in understanding the needs and concerns of the next generation. This leads to a sound understanding of their inner selves leading to higher accountability of their actions. The contrary is bound to happen in cases where the senior generation is authoritative and less empathetic to the next generation.

6. Summary

Succession planning is an extensive process that covers in its ambit a range of decisions pertaining to the owner, the successor/s and the organization as a whole. Estate planning is a sophisticated process that requires the owner to make provisions with respect to assets and investments in a way that it attracts minimum taxation liabilities at the time of the transfers post the death of the owner. Succession cannot be forced, it has to be considered as an opportunity and not as a liability. It requires the successors to understand their own aspirations, they should be able to see a future and self-development with the firm and should be come as a natural instinct. It will happen only when the senior generation prepares and makes provisions for a smooth induct and continual journey for the successive generations.