Succession Planning Versus Estate Planning

Family businesses struggle with differentiating succession planning and estate planning. Both are critical strategic issues that merit thought and action when building a successful business and financial security.

Succession planning (also called transition planning) is comparable to business life continuity planning. It deals with critical questions related to the continuity of the family business, such as:

- Is this business viable past the current generation, or should it be liquidated or leased to provide maximum liquidity and security for the current operators?
- Are there interested and competent successors who can carry on leadership if the operation continues?
- Who will provide the capital in the next generation—successors not actively engaged in farm management or only actively engaged successors who own farm capital?

To answer these questions, family business stakeholders need to hold family meetings and consult with their team of advisers. As the issues are discussed, honesty is a must. For example, do family members who are considering entering the business have a shared mission, vision and commitment to common values? Often, potential successors are skilled operators but lack essential skills and interest in management and leadership; who will fill those roles in the future? Is merit the criteria for involvement or entitlement? What is your family employment policy toward apprenticeships away from the farm?

Estate planning deals with a connected but different slate of issues and is similar to death planning. It address elements such as:

- Financial wealth assessment
- Estate tax exposure
- How much wealth is needed to provide security until projected death of the principals?
- How much of current wealth is in excess of needs for financial security?
- How much of this wealth should be distributed before death versus passed upon death?
- What is the current status of insurance and investment portfolios?
- How will investment strategies need to shift if business transition results in new investable funds having to be managed (i.e. from sale of business investments)?
- What are intentions for final health care directives and distribution of personal assets?
- When should retirement plans and social security payments begin?
- Have you shared your financial picture and estate planning decision challenges with your heirs and asked for input on how to address these issues?

The biggest mistake I've witnessed in four decades of advising family businesses is the tendency to start with estate planning, with best of intentions to work on succession planning later. These planning processes can be tackled simultaneously. But, until the succession planning questions described above are answered, it is difficult for any competent adviser to effectively counsel a client on the optimal estate plan. Objectives and strategies for optimizing a transition plan will play a critical role in determining the optimal strategy for designing an estate plan. Failure to address these issues in the right order has disastrous outcomes.

Both succession and estate planning are critical issues high on the list of priorities for stakeholders looking at exit/retirement plans as well as prospective successors trying to determine if the farm is where they want to pursue a vocation and financial investment. Don't be afraid to tackle the questions and issues in each of these camps, but be careful not to put the cart before the horse. **FJ**

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