

Work Samples Series

The Assignment:

MarshComm was contracted to write two articles for Jefferson Pilot Financial's *Partner* magazine, published to provide sales strategies to its field agents and financial representatives.

The second article, below, is a feature on succession planning for small businesses, the theme of the issue. This article features personal insight and a number of first-hand accounts of successful succession planning by Jefferson Pilot agents.

Succession Planning Vital for Small Businesses

Agents' advice, stewardship and utilization of insurance products are the keys to ensuring their clients' succession planning needs are fully met

Bill White first approached his long-time client Roger Jennings several years ago about developing a succession plan for Jennings & Company, his PR and advertising agency. White, the owner of Chapel Hill, N.C.-based William R. White & Associates and a 38-year industry veteran, began the background discussion by asking Jennings his customary attention-grabbing question: "What's going to happen to this business when you die?"

Like many small-business owners, Jennings had never consciously reflected on the question himself – loaded as it was with many unsettling implications. But now he credits White with pressing the subject. "Bill is always posing the tough questions and forcing me to think about these sorts of issues," says Jennings.

The answer to that essential question, and a number of other related queries, forms the font of information from which insurance agents – and associated financial, tax and legal professionals – can begin to formulate a succession plan for their small-business clients. Succession planning is an often overlooked, but essential, element in the successful transition of a small business after the owner retires or dies.

Kevin Metzler, a 24-year veteran agent and part owner of Buckley & Company Financial Services LLC in Lexington, Ky., cites the woeful record of small family business succession to drive the point home: Less than 30 percent of family-owned businesses are successfully transitioned to a second generation of family ownership, and less than 10 percent to a third generation.

The reasons for this are straightforward, according to Metzler. “Most small-business owners don’t do the proper estate planning or succession planning,” he says. “Often, the estate tax burden – fueled by a high valuation of the business by the IRS – takes the business into negative cash flow or forces the heirs to sell the business to pay the estate taxes.”

Metzler offers his clients a unique approach to learning about succession planning: a video-driven seminar called “Business Killers.” The seminar features a video in which actors take participants through six different scenarios that could “kill” a small business. The actors play out the scenarios to their likely, unhappy, conclusion, then offer the solutions that can prevent a real-world occurrence.

Metzler facilitates the seminar, introducing the six vignettes and discussing the insurance products and services that form the basis of many of the solutions. Typically, he has a lawyer on hand to offer legal advice and – like all insurance professionals who work on succession and estate planning – insists that a CPA or tax expert be involved to handle the myriad tax issues.

The six deadly succession sins played out in the video are:

- 1) **“I know what my business is worth,”** highlighting the importance of a formal appraisal for a small business;
- 2) **“I’m too busy running the company,”** stressing the need for a detailed, written succession and estate plan;
- 3) **“That will never happen to me,”** on the importance of disability insurance in addition to life insurance;
- 4) **“There’s plenty of time for that,”** on the evils of procrastination;
- 5) **“My business *is* my retirement,”** focusing on the owner’s need to diversify investments beyond

the business itself; and

6) **“You can’t beat Uncle Sam,”** encouraging the use of a tax professional for strategies to reduce the business and estate tax burden.

Tim Johnson, owner of Terry Johnson & Associates Inc., a Fayetteville, N.C., insurance agency, is a second-generation example of how to execute a successful family business succession plan. Five years after graduating from college, Tim joined his father, Terry – who was 35 years into his 50-year career – in business. The year was 1985, and the first thing the Johnsons did was set up a clearly defined succession plan.

Neither his brother nor sister was interested in participating in the business, so Tim and his father put in place a buy-sell cross purchase agreement funded with life insurance. Upon Terry’s death, through the insurance coverage and the purchase agreement, Tim would assume ownership of the business while his mother would receive, tax-free, the inherited wealth from her husband’s 50-year stake in the business. Tim’s brother and sister would inherit their share of this wealth upon their mother’s death.

When Terry died in 1999, the well-structured succession and estate planning worked perfectly. “Life insurance,” says Tim, “allowed a smooth transition and satisfied all parties involved. It is the single most important succession planning tool, because it begins and ends every plan.”

Tim Johnson’s personal experience with succession planning underpins the process he follows when assisting his clients with their own succession plans. “I try to put myself in their shoes,” he says. “And I ask a lot of questions.” Among them are:

- How did the business get started?
- How did it evolve to get where it is today?
- To what extent is the family involved in the business?
- If the owner has children, what would their involvement be if the owner dies?

The questions point out an important facet of small-business succession planning – it is an evolutionary process. “It starts from Day One and becomes more complex, with various needs

arising as the business matures,” Johnson says.

For example, when an individual starts a business (without much, if any, equity built up, depending on the type of business), insurance might just cover the owner’s potential earnings, essentially guarantying the economic security the business represents at that point to the owner’s family. However, when the business matures, equity builds and more employees may join – raising a host of new estate tax and distribution planning, key-employee, executive compensation and other issues that only life insurance can address.

Sometimes the evolution takes place from one day to the next. Bill White worked with Roger Jennings to structure a succession plan that would allow a key executive of Jennings’ PR and advertising agency to buy Jennings out in the event of his death or upon retirement. They set up a buy-sell agreement through a lifecomp policy that insured Jennings. As the beneficiary, the key executive was provided a bonus that covered the PS 58 costs (the economic value of the death benefit reported to the government), but the policy – and most of the accumulated cash value – belonged to the business.

Almost seven years into the agreement, the key executive abruptly left the business, frustrating Jennings’ best-laid succession plans. He did, though, retain ownership of the policy and most of the cash value. In the meantime, Jennings’ daughter had graduated from college and started her own career out-of-state. She joined him in the business five years ago, and the Jennings are now structuring a new succession plan that will allow her to become owner of the business over time.

Which introduced yet another issue to be addressed: How do the Jennings keep and attract key executives who no longer have any ownership potential in the business?

One way, says White, is to offer them a supplemental executive retirement plan (SERP). Typically funded with a universal or variable life plan, the business pays the entire cost of the plan and pays a bonus to the executive to cover the PS 58 costs and accumulate dollars for the executive. If the company performs well over time and contributes healthy premiums to the plan, the executive can

retire with a normal retirement plan (401(k) or IRA), Social Security, and have full control of the SERP as a supplement to this income.

Jennings credits his and White's 30-year business and personal relationship with White's ability to continually deliver the solutions to meet the often fluid needs of his business. "He knows my personal situation and my business situation," Jennings says. "In many cases, he's able to anticipate my needs.

"I'm 60 years old, and a lot of these issues are pertinent to me now – retirement and estate planning, an exit strategy and succession planning," Jennings continues. "They're certainly all tied together at this point in my life."

Kevin Metzler distills to its essence what it means to business owners like Jennings to adopt a succession plan. The peace of mind alone is invaluable.

Says Metzler, "They can sleep at night knowing they or their heirs will get the full value of their business and it will continue to operate in the manner they chose."

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