



***PRESERVING THE LEGACY  
OF A FAMILY-OWNED BUSINESS***

**A PSYCHOLOGY OF  
BUSINESS SUCCESSION AND ESTATE PLANNING**

by  
**Tim Bachmeyer, Ph.D.**  
and  
**William A. Snyder, J.D., L.L.M.**

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This book is not intended to provide legal, accounting, financial or other advice. Readers are urged to contact qualified professional advisors for their legal, accounting, financial, or psychological/communication needs.

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## PREFACE

This book introduces a dimension to the estate-planning process that will be familiar to the reader's experience—but not because of his or her professional or business training. Rather than create a book focusing strictly on the technical side of estate planning, we treat estate planning as a series of emotional decisions by clients that later become formalized in a logical, technical plan crafted by a client's team of advisors.

This book is an analysis of both the emotional and communications aspects of the estate planning process within a small business family. We have created the composite case of a typical family owning a small business—the Bakers—taking them through each step of the estate-planning process. This is a narrative told not only from the traditional, exclusive point of view of their attorney but from the Bakers' own point of view as well, including their goals, their hesitations, their dreams and their fears. This stands in contrast to approaching estate planning from a set of “facts” from which a professional advisor creates a logically constructed plan based on professional expertise alone. In our approach, the feelings of Bob and Sue Baker, their concerns about the succession of the family business, Baker Pumps, their relationships with their adult children, and their concern for leaving a family legacy are the clay out of which their estate plan is sculpted. And as their attorney addresses each of these concerns in turn, he crafts a plan grounded in the lives and needs of his clients, not in the logic of taxes, trusts, and numbers in which he has been trained. As you will see, these so-called “hard” considerations are crucial in the Bakers' plan but are subsidiary to the goals they seek to identify and clarify as they work with their attorney.

This approach to family estate planning is both comprehensive and integrated. First and foremost it balances the needs of both the Baker family and the individual members within the family system over three generations. Second, the creation of an estate-planning package integrates these needs with estate-planning solutions uniquely tailored to the family's concerns. Just as there is no one—perfect family there is no one perfect family estate plan.

**This approach to estate planning is by necessity a team approach.** It involves not only an estate planning attorney, but also an accountant, a financial planner, a business succession planner, a life insurance agent, trust officers, and charitable planned giving officers. As the reader will see, in order to achieve the optimum results for the Bakers, each of these professionals will have an important role in fashioning some aspect of a comprehensive and integrated estate plan.

Many of the estate-planning tools utilized by the Bakers will be familiar. Here they have been applied to the Bakers' unique situation, that of a family with a small business wishing to preserve its legacy. We recognize that there is never a single formula for estate planning and that there are many variations to meet a particular business or succession need. Consequently, at particular points in the text, we may refer to a well-known, prominent vehicle even though it may

not be the optimal choice for the Bakers' situation.

We find the Bakers' overall goals quite typical. They are a couple with a successful business that they hope to pass to the next generation while securing their retirement. *How* they will achieve this, however, is their unique story. The Baker family is by no means a perfect family. They appear to have the often-found conflicts between the first and second generations, some relationship difficulties within the children's families, and a lack of clearly-defined business-succession goals. To their credit, however, Bob and Sue Baker are willing to face their family and business-succession issues directly.

In contrast, what financial-services professional hasn't seen family and succession problems simply ignored by their clients? Or seen the best-crafted estate plan, will, or charitable trust simply disregarded or unfunded by their client? Or worse yet, witnessed squabbling among the generations that effectively sabotages any attempt at planning? The advisor may know that the plan in question will suit the client perfectly and has designed it to save the client thousands of dollars in both income and estate taxes, yet the client—whatever his or her own wisdom—ultimately fails to act. And how often have attorneys been frustrated by clients who insist on punitive clauses in their wills or estate plans or who demand trust provisions to carry out some long-held personal agenda that will vindicate them (they believe) from the grave? How often have attorneys and accountants had to “clean up” estates of clients whose “I'll take it with me” insistence resulted in added financial turmoil placed on the shoulders of their families at a time of vulnerability and grief?

Among families with small businesses, a frequent concern is the failure of the head of the business to have taken the time to develop proper estate or succession planning—with the consequence that upon his or her death in order to pay estate taxes the business is forced to sell and consequently is lost to the family. The founder's life work then vanishes, and the family legacy disappears. Or the estate ends up embroiled in financial and tax-related arbitration that concludes with the federal government being the final and sole beneficiary of the founder's life work.

Estate planning is motivated by the whole spectrum of human emotions. We affirm this by defining estate planning in a new fashion: **Estate planning is a series of emotional decisions formalized in a logical plan created by a professional advisory team and communicated among family members to optimally ensure the considered feelings, beliefs, and goals of the testator.**

By “emotional,” we do not mean “irrational.” Feelings have a logic of their own, and it is this logic that the professional advisor must take into account if he or she is to provide optimum counsel.

Our experience is that many professionals frequently recognize emotional signposts of clients and families struggling to plan for the future of a business without its founder. Yet most of these same professionals are uncertain how to intervene in these delicate matters. Unsure of their own credibility with their clients, or out of fear for making an embarrassing intervention

and losing a client, they remain silent and rely on what they know best, a well-articulated but logical plan that they hope will address the facts their clients present to them—absent the family emotions.

The good news in this situation is that most professional advisors already act in the sanctioned capacity of a counselor or guide. This is their socially authorized function. Our belief is that this advisory role can be expanded without violating professional boundaries or turning advisors into psychologists or therapists. In addition, there will be instances when a professional will refer clients to professional succession-planners or family counselors just as they might refer them to another ancillary professional. Certainly, attorneys, accountants, financial planners, trust officers, planned giving officers, insurance agents, investment advisors, and even business appraisers all regularly refer their clients to one another. Recommending the use of a professional skilled in family problem solving is no different, as we shall see.

In the case of the Baker family a specialist trained in communications plays a key role in their planning. Assessing the relationships within the family, their attorney sees the need to address them directly. In order to lay the foundation for an effective business succession and estate plan, the attorney and communications specialist together conduct a family retreat with two generations of Bakers. Focusing on the issue of business succession first, the Bakers find solutions to emotional and relationship barriers within their family. These in turn facilitate—and actually enhance—the discussion of their formal estate plan.

Just as a computer program branches out into a full design far flung from the original starting point, so flows the estate-planning process. We view this process as a series of decisions with many branches. The “root” or core decisions are clearly emotional ones. **This does not mean that these decisions lack reason or logic, but that they have an emotional component that shapes and colors individual reasoning.** The best solutions to these emotional considerations are logical; but the logic of any plan must take account of the emotional situation of the client in order to achieve the intended goals.

The situation of the Baker family provides guideposts at each decisional branch an estate plan might take. We have included most of the sophisticated estate-planning techniques in use today. Considering the myriad tax changes brought about by the Economic Growth and Tax Relief Reconciliation Act of 2010 (the “2010 Tax Act”), not every technique will be explored here; however, we believe we have covered the most significant ones. Specific chapters address the important concerns or roles of a variety of estate-planning professionals: not just the estate planning attorney, but the C.P.A., financial planner, succession planner, life insurance agent, trust officer, investment advisor, and charitable giving officer. We have shown how a typical family of means whose main asset is a family business moves through the estate-planning process, successfully dealing with their emotional agendas and communication challenges as they encounter professional concerns at each step.

**With the degree of uncertainty introduced into estate planning with the provisions of the 2010 Tax Act, issues of communication and family relationships are underscored more**

**now than ever before.** The changes recently introduced into the technical side of planning remind us that good planning begins with good relationships. Conversely, difficult family relationships create a difficult environment for planning.

It is our opinion that the solution-oriented approach to communication and planning advocated here is particularly suited to the new estate tax environment. Because of the new Tax Act changes, many children and grandchildren taking over a family-owned business will never pay estate taxes. This does not eliminate the need for planning, but to the contrary provides the incentive all the more for opening lines of communication, creating a broad sense of ownership, and incentivizing accountability in all family members as they consider preserving the legacy created by an entrepreneur and spouse.

We hope that clients and advisors alike will find this book extremely helpful. Neither of the authors could have written this book alone. We both found we needed one another's expertise in order to balance technical and non-technical factors in succession planning. Combining Bill's 40 years of estate planning with Tim's 10 years of private psychotherapy practice and 28 years of charitable gift planning will provide the reader with what we hope are the benefits of substantial professional experience. We have created it as the sons of small business families. Each of us was shaped by the experience of growing up in a family-owned business. Having the "family business" as a member of the family is a truly unique experience.

This is the story of a hypothetical family. Yet goal setting, conflict resolution, estate formulation, and the identification and preservation of a legacy are typical characteristics of a business family in transition. In all families, change is constant. Individuals are at different stages in their own personal growth, family relationships are in different stages, and the family itself has its own developmental stages. This study addresses family needs as a whole but with reference to the individual and relational dynamics that make up the Baker family.

Each chapter concludes with reflections about the issues discussed in that chapter. We intend for the book to be a guide that captures the estate-planning process for both the individual and the professional advisor. We assign details and technical matters their rightful importance but are aware they can distract both the advisor and the individual from the true purpose of estate planning—that of achieving the goals of the client. Our vision for individual and advisor is a collaboration which keeps in mind the emotional and communications dynamics that underlie the estate-planning process and which, when properly addressed, can optimize opportunities and satisfaction for client and advisor alike.

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*Fort Lauderdale, Florida*  
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## Chapter 1

### THE BAKERS:

## An American Family in Transition

### An Entrepreneur and His Legacy

Bob Baker embodies the American Dream.

Bob is a self-made millionaire. He owns the company named after him, Baker Pumps, a C corporation he started thirty years ago. It is a leading manufacturer of marine pumps and does \$3 million in business annually. Baker Pumps is quite successful, netting a pre-tax profit of \$300,000 each year.

Bob is 62 and has been married to Sue, 60, for 40 years. They have three children. Sue has never worked outside the home and has dedicated herself to raising their three children and (as she occasionally jokes) Bob as well. The children are now grown and have pursued their own lives. Joe at age 38 is the older son and lives 300 miles away in a major metropolitan city. He has become a successful and distinguished architect. He is married, and he and his wife have a newborn. Their younger son, Jim, is 32. He is married and has two children. Jim is very involved in the family business, having worked in it since he graduated from college. The middle child, Jane, aged 33, is much like her mother—a married housewife and also the mother of three children. She and her family live in Fort Lauderdale not too far from her parents. The Bakers have wealth and happiness and are the envy of many of their friends in their church and community.

Yet on the horizon Bob sees problems that worry him. His financial advisors have been pestering him to develop a business-succession plan, a prospect he does not relish for several reasons. To begin with, Bob sees himself as a hands-on engineer. He knows pumps, he knows engineering, and he knows business. He's comfortable with numbers and P & L statements. But considering what to do with the future of his business—and his future—presents him with parameters with which he is unfamiliar and uncomfortable. Also, and just as important, he feels overwhelmed and has no idea where to even begin thinking about such an enormous undertaking.

Bob Baker *is* Baker Pumps. His identity is totally involved in his business. To a casual observer, he might be seen as having an exaggerated sense of self-importance; yet his sense of vision, personal perseverance, and deep self-confidence have made him the success he is. His strength of personality has carried Baker Pumps through many a financial storm, and with each crisis his confidence and sense of purpose have grown stronger. After all, he created the

business, nurtured it, suffered its ups and downs and is responsible for its success. To think of his business without him is—well, unthinkable.

Furthermore, Baker Pumps is booming. Its revenue and income sales continue on a upward trend. Experts are saying Baker Pumps is becoming an industry leader, a prospect Bob never dreamed of when he started the business with a \$10,000 loan from his parents. The notion of this level of success makes Bob enormously proud. While he would not in his best moments say he is “attached” to it, the prospect of a life apart from his business is simply foreign to him. Bob’s lifelong goal has been the success and growth of his company—he lives it and sleeps it. In fact, his total commitment is the reason for its success. In considering a business-succession plan, Bob would have to face letting go of his business, a prospect that would deeply sadden him. The business has become such a part of him and he such a part of it that it would be akin to losing a child. Unlike many of his contemporaries who are quietly asking the same questions themselves, Bob cannot avoid the question of the legacy he wishes to leave. Baker Pumps is his legacy. His investment in seeing it thrive and live beyond him is enormous. While he is ambivalent about thinking of Baker Pumps minus Bob Baker at the helm, he is even more motivated to have a thriving Baker Pumps existing long after he passes on. The prospect of leaving a legacy is part and parcel of Bob’s identity.

## **The Storm Clouds of Business Succession**

Bob will also have to face other major decisions such as the role his children may (or may not) play in the future of his business. He will need to assess their capabilities and their levels of interest. He will need to discuss with his wife areas long left—by mutual consent—undiscussed, such as the immaturity of their younger son and what has become the alienation of their older son. And while their daughter is devoted to her parents and brothers, all is not well within her household. Her own family problems might limit any role she could play in the succession of Baker Pumps to the next generation.

To add an additional concern, Bob has been worrying about his health for the past four years. This began when his father’s triple by-pass surgery left Bob with the realization that he himself is not invincible and that sooner or later he will need to think about slowing down. His annual checkups at the Goodall Clinic have given him a clean bill of health each time; but *as* Sue reminds him, stress is an ever-present factor in his life. His anxiety about his business’s future has kept him awake nights. Further, his best friend and golfing partner, Bill Edwards, just suffered a severe and disabling heart attack. A close friend of theirs from church discovered six months ago he had contracted prostate cancer. Bob has always considered himself luckier than most, but in the back of his mind he wonders if disabling illness might strike him. Sue’s reminders that he should begin to slow down and “smell the roses” and enjoy the fruits of his hard work make it all the worse. He wants to ease up and enjoy those fruits, yet quietly worries that the business would suffer without him. While he is wistful about the time he spent with his business throughout the years instead of with Sue and the kids, the second home he and Sue have in the Florida Keys now provides solace from these anxieties and has become a rallying spot for

the family during holidays and winters. Jane and Jim and their families regularly get together with Bob and Sue in the Keys. These are times Bob truly relishes. Bob nostalgically remembers to this day the Labor Day Joe and his wife joined them for a real family get-together. The memory becomes all the more poignant as Bob reflects how close the family might have been if he had shared more time off with his family as they were growing up. Bob and Sue also see the Keys home as a sanctuary from the hustle and bustle of life and a rare piece of “pure nature” that is hard to find in America anymore.

Sue has been Bob’s close companion and emotional supporter since they first met in college. While by mutual consent her job has always been to raise the children and take care of household matters, Bob has never viewed her work and role as secondary to his. As a matter of fact he was relieved that she took over the majority of parenting matters, since deep down he didn’t feel especially qualified in that area. This easy division of roles has had its problems, however. While Sue has always been interested in the family business and offered her views when asked, she is not conversant with its technical or financial complexities and has no desire to be so. As Bob contemplates what role she might play in his business-succession plan, he is at a loss. The marital division of functions that has served them so well appears to be problematic for the future he is contemplating for his business.

## **Resources for the Transition**

As Bob starts thinking of his children and their roles in the future of his business, he feels he is on uncertain ground there as well.

His oldest child has followed in his footsteps in that he is highly successful in a technical occupation. Joe designs award-winning buildings and has made something of a regional name for himself in architecture. Like his father, he is totally devoted to his work and is extremely busy. He is not close to his siblings, and so it is easy for him to use work as an excuse to avoid the annual family get together in the Keys. His mother wonders if perhaps Joe is jealous of the close relationship his younger brother has with their father through the family business. His only communication of this possible resentment is unavailability for the family outings that his parents cherish more and more each year as they grow older.

Unlike his older brother, Jim is close to his parents. At work he is a chip off the old block. Each day he arrives early to work, sometimes getting there even before the true early bird, Bob, arrives. Bob appreciates his son’s natural intelligence and his eagerness to learn, but wishes Jim would be more independent in his decision making. When Jim comes to him with supervisory problems at the plant, Bob tries to elicit as much of Jim’s independent thinking as possible. While Bob came up the hard way, he realizes that Jim has been given the best—a top education, his first car while in high school, a job in the family business. He has never had to take risks or face the financial valleys in life his parents have, which they believe made them strong. Bob sees Jim as his natural successor in the business but wishes he were more mature, more experienced. Now Bob is uncertain how to train him to become more independent and stand on his own two

feet. Jim is a good husband and parent, but his personal values are not those of his parents. He relishes the outer signs of success—the flashy car, the European clothes, the fancy jewelry—that Bob has always avoided. Bob owns a simple Seiko watch and drives a 5-year-old Buick. Bob is uncertain how to assess his youngest child's capacity for mature judgment, especially the judgment to manage the successful trajectory on which Baker Pumps is about to embark.

Jane, the only daughter, is still her mother's pride and joy at age 33. Bob never was sure just how to relate to a daughter and always felt relief that Sue knew how to raise a girl. Jane was the girl her mother always wanted, and Sue tended to dote on her more than her sons. Jane grew up especially close to her mother and, like her brother Jim, went to the college her parents attended, the University of the Southeast. To her parents' dismay, she married Jeff, a classmate whom they considered under-motivated and whose influence on Jane they still cannot fathom. At first, Sue and Bob were overjoyed when Jane and Jeff came to live in Fort Lauderdale to raise a family, but these sentiments gradually turned to concern as their daughters' marriage began to show signs of strain. The silence between them at family gatherings was uncomfortable and Jeff's drinking became an embarrassment for Jane and their children. Yet Jane seems to persevere and make the best of things. Although Jane still remains particularly close to her mother, she has never discussed her problems with her father. As he considers his business and family legacy, Bob keeps coming up blank for any positive role Jane might play in his considerations.

All the while he has been in his business, true to his engineering training, Bob has always looked at problems from every possible angle before making a decision. Deciding what to do with his business is an entirely different game altogether, though. While Bob's great intuition for business has enabled him to take the right risks at the right time, as he looks inside himself for that inner guidance he could always count on, for the first time in his life he is uncertain. There are so many pros and cons concerning Jim's abilities that he feels torn. And in considering a succession plan, there seem to be so many variables and risks that could endanger his whole life's work. The temptation to keep absorbed in work and to avoid the whole problem had been easy to follow until illness struck his father and his closest friends, causing him to face his mortality.

The risk of inaction is not one Bob cares to calculate either. The \$6.0 million in stock in the family business is in his name only. The dream home that he and Sue built years ago has a market value of almost \$2.0 million, as does the commercial property that houses Baker Pumps; his I.R.A. has an account balance of \$1.0 million in marketable securities; his brokerage account has another \$7.0 million in it consisting of low-basis, highly appreciated marketable securities whose total annual return has been about 6% for the last 10 years; and the Keys property is now worth \$2.0 million.

Bob's C corp stock has significant accumulated earnings too. Obviously he has handled his money very well. He and Sue have raised three children in solid fashion, sending them to college and even helping Joe with an advanced degree in architecture. The mortgage on their first home is paid off, as is their second home in the Florida Keys.



If you asked Bob what his net worth is, he could give you a figure; but he is so busy running his business that he never stops to count until he meets with his C.P.A. at year's end. In addition, he likes to think of himself as always in control. Life has its ups and downs, but he has always believed that he has had more luck and talent than the other guy. And as his own boss, Bob has always relished the control and freedom he has had in his own life. Bob would be lost having to report to someone else. The sense of freedom to do things his way, to be *the* boss, is absolutely thrilling to him. And to have the total responsibility for a \$6.0 million company, even with all its risks, is the closest thing to an adrenalin rush Bob has ever experienced.

Yet, his own aging and the health problems of his friends and peers are threatening Bob's sense of success and control over his life. His memory isn't as sharp as it used to be. His agility with numbers is slipping. Each night when he retires, he can never count on a good night's sleep. And perhaps worst of all, the sense of inner confidence that has been with him since his youth is slowly diminishing. In addition, because of the publicity surrounding the 2010 Tax Act and its possible implications for small-business owners, Bob decides to schedule an appointment with his attorney, Fred Scott, for Monday morning.

## Reflections

1. As Bob Baker calls his attorney, it should be clear that Bob and his business are inextricably intertwined and that to him absolutely everything he is, not just owns, is at stake.

2. Compared to someone of lesser means, Bob's preoccupation with loss is higher and his anxiety over making estate decisions is higher because of the risks involved. His level of assets do not shield him from worry. If anything, they exacerbate it.

3. If you were Bob, what would it take for you to trust your advisers with such risks at stake? Bob has faced risky situations before, but entering an overwhelming situation with so much at stake *personally* is the largest challenge he has ever faced. Fortunately, he can rely on his innate intelligence and intuition, resources he has used in the past. The bigger challenge, however, is to find ways to reassure himself about personal risks (family relations, his health, the legacy of his business) that his business commitments have preempted for years.

4. The most important thing for Bob is to have a sense of security and continuity as he evaluates and transfers the business. To do this he needs to find and hire the right professionals. Bob does have a basic confidence in his attorney who has helped him with business dealings in the past. Absent this, his past experience in hiring managers or employees, his intuitive skills about people, and a network of friends and business associates will serve him well in selecting the right advisors.

5. To those outside the family, the Bakers present an ideal family portrait. However, in reality there is no such thing as a perfect family or one without problems. What has been Bob and Sue Baker's strength in the past is not that they have been problem-free but that they have faced conflict and problems and worked them through to the best of their abilities.

6. Like many other small business families, succession planning brings forth a host of issues that are part and parcel of every family's life. Whether these issues are familiar or completely new, the Bakers have inherent resources in their family system, as we shall see, that can bring them to new and effective solutions.

## Chapter 2

### SEEKING PROFESSIONAL ADVICE:

#### Personal Rapport and Professional Credibility

Sitting in the office of their attorney, Bob and Sue Baker are having very different thoughts as they wait for their appointment. They look at all the law books neatly stacked on shelves that almost completely surround the office. Bob thinks about how much money this estate planning is going to cost him. He personally likes Fred Scott, but he has always been reluctant to go to him because of the cost. Rather than pay legal fees, Bob feels he can better spend his money producing more revenue for his business. He knows he needs to decide what to do about its future, but he wonders if using an attorney will be worth the time and money he could be using for what he truly wants to be doing: keeping Baker Pumps ahead of his competitors.

Sue's reaction is quite different. She too has reservations, but for her it's that she is in unfamiliar territory. She has not been part of the professional relationship with Fred that her husband has enjoyed over the years. Nor is she well-versed in the details of the business. Any reluctance, though, is more than outweighed by her relief that Bob has finally agreed to talk to someone about the issues that have been keeping him awake at night. Indeed, she is anxious to begin the conversation with Fred.

#### Establishing Rapport

Bob met Fred Scott almost fifteen years ago while playing at a member-guest golf tournament at Fred's country club, a rare occasion when Bob permitted himself to get out of the office. Fred is well-versed in business and estate planning and has an advanced law degree, an L.L.M. in estate planning. He is also board certified by the State Bar Association in wills, trusts, and estates. He lectures throughout the state to attorneys, C.P.A.s, life insurance agents, and business planners on various subjects dealing with estate and financial planning.

Fred's credentials do not allay Bob's worries, however. Fred has been after Bob to do estate planning for the last several years, and whenever they meet the subject always seems to come up at Fred's initiation. Bob is more apt to feel in control if he initiates any new ideas. Just by accepting Fred's suggestion, Bob already feels he has lost a small battle. However, he knows he must do something about his worries and sleeplessness.

The meeting begins on a relaxing note as Fred enters the room and introduces himself to Sue. He reminisces a few moments with Fred about how they first met on the golf course and

goes on to ask Sue about herself, their children, and her own interests. From his years of experience, Fred knows that taking time to exchange pleasantries and get acquainted is a very important step in building rapport. Bob and Sue have their own separate concerns and are wondering just how Fred will be able to address them. Credibility and rapport are important issues right from the start.

Fred acknowledges to Sue his and Bob's long business relationship, but he makes a point of explaining that estate planning is quite different from business planning. While the former includes their business, estate planning is a much broader enterprise, since it concerns not just the business but everything Bob and Sue have acquired over their lives together. Additionally, it involves considerations about their family relationships and Sue's opinions are essential to creating a successful estate plan.

Fred opens the discussion of business by acknowledging that when clients come to see him, they always have something important on their mind. What might that be in the Bakers' case, Fred wonders. "What prompts your visit today?" he asks.

## **Plunging In**

In his typical manner, Bob charges ahead. "Baker Pumps is like a pot on a stove ready to boil over, Fred. It's growing like mad. But I'm thinking I'd like to back off, turn down the heat. Jimmy's a good kid, but he's not ready to take over, and I don't think the other kids can help either. Something's got to be done!"

Bob continues, "You see, Fred, I'm not getting any younger. Joel Leventhal, my C.P.A. is saying the time is right for dramatically expanding the business. That's a big undertaking. I've been thinking personally about how to cut back, not to get more involved in the business. It would be great to put Baker Pumps on the map, but I just don't know. Sue has been after me to spend more time with her, but who would run the business? And now seems to be the worst time to cut back. Any ideas?"

A true engineer, Bob has given a very logical and precise analysis of the problem. And while being quick and to the point, Bob has obviously not shared all the worries and concerns that are keeping him awake nights—worries about his health, for instance. Bob does not need to put his entire emotional agenda on the table. From his emotional tone and the quickness of his explanation, Fred infers the level of importance Bob is putting on this discussion. Fred also knows that over time, as the estate-planning process unfolds, other agendas will come forth much like a line of cars on a freight train. By establishing rapport with the Bakers, Fred knows that he won't have to "dig" for these other issues; they will come out naturally as their discussions evolve.

Communicating this understanding, his technical expertise notwithstanding, is the most important thing Fred can offer his clients. While empathy is an intangible, Fred has found it is crucial in making the estate-planning process go as smoothly as possible. Indeed, his empathy

invites a level of trust from his clients that in turn enables them to be open with their concerns. One of the reasons for Fred's success as an attorney is that he understands this and, without being intrusive, he always tries to see things from his client's point of view. Fred also has the wisdom to jot down each client's very first words, having found that they almost always form the basis for a recurring theme throughout the entire estate-planning process. Fred knows that if he discounts anything a client first mentions, it will surface sooner or later in the discussion and, if not addressed, may sabotage considerations at just the wrong time. As he makes his notes, he delineates the questions that he will have to answer for his client if he is to be successful. In the Bakers' case, Fred simply notes, "pot boiling over," "grow or back off?" "who will take over?" "B. Pumps on the map," "time with Sue," "who to run business?," "cutting back." It will be these first words that will set the direction of their motivational agenda.

In working to establish rapport with his clients, Fred is already off to a credible start. Chatting about small things first helps initiate a workable relationship. Fred has another advantage as well. By nature he is a warm person who likes his work and his clients. Consequently, he communicates a positive attitude in all that he does. This warmth helps Bob and Sue—who are in a new situation with much on their minds—to relax and begin to gain trust in him. And while Bob has known Fred for many years, this is a new aspect of their relationship—Bob has never needed to count on Fred's advice with so much at stake. In this first meeting Bob and Sue are testing the waters and checking Fred's credibility.

Because of previous work he has done for Baker Pumps, Fred already has a rough idea of Bob and Sue's financial situation, but he needs more information in order to proceed. While it would be easy for him to simply hand over the Client Information Sheet he gives to every client, he decides not to do so at this point. The form consists of some twenty pages requesting complete financial information on assets starting with cash accounts and ending with business interests.

## **Creating a Climate of Empathic Understanding**

Fred has learned that an abrupt presentation of a form asking so much information can be a bit chilling and can turn clients off even before they get started. And intuitively he knows that in the give and take of the discussion of estate planning, it is better at the beginning for him to be a giver rather than a taker. He knows that Bob is already worried about how much this is going to cost him (what he's going to have to give up), and the more complicated the discussion gets, the more his worries will increase. So Fred instead responds with a statement affirming at many levels the concerns Bob and Sue have brought with them.

"I know how much Baker Pumps means to you, Bob, and I have an idea of just how much Bob and your family mean to you, Sue. Deciding what to do with your business at this point is a pretty big worry, and your decision will impact both of you and everyone in your family. A number of my clients have considered expanding their companies or even taking them public. Some have and some haven't. And to be honest, it's a bit nerve-racking at first. I know you're a

results-oriented kind of guy, Bob, and you like to look at things from every angle and then move ahead at full speed. That's great, because we need to look at things from every angle together to produce results you'll be happy with. But even more important are the goals you and Sue have for one another and for your family. Your business is the center of your family life and of your financial security. You are at a point in your lives where you need to think about what you want to do next: cut back, as Bob says, retire, pass along—or perhaps—even sell your business. The best thing we can do today is to talk about your life goals and how the business fits into them. While at first it may seem we're not getting anywhere or even taking detours, I assure you that being clear now on your long-range objectives will pay off handsomely in time, effort, and money. I will be very careful of your time. My clients have found they can save themselves and their families a lot of money by investing a few dollars up front in planning their estates properly. No one likes to pay taxes, and as a small business owner you know better than most just how much the government likes to keep its hand in your pocket. No doubt you want to minimize the government's share of your estate? (Bob readily nods in agreement). And there are many options available for you to save yourself a lot of trouble and money at this point in your lives. To be effective, an estate plan should include not only your children, but their children as well. We're really talking about a three-generation plan. So let's begin with the big picture: what you two want out of life for as long as you have one another?"

"Before we get going, how much is this going to cost us," Bob asks, shifting the topic to what is uppermost on his mind. "In spite of your assurances, it sounds like a pretty big undertaking."

"My fee is \$350 per hour, and my associates charge at a lower fee for less demanding work. There may be fees charged by other professionals as well. What you should keep in mind is that together we are creating a plan for your future. And while the business component is a large part of that, we really are talking about financial and estate plans to take care of yourselves, your children, and even your grandchildren. As we progress, I can give you a better idea of the number of hours involved." Bob and Sue nod in agreement.

## **Goal Setting**

"So let's focus first on your goals," Fred continues. "What are your priorities as we sit here now?"

"My biggest concern is Baker Pumps," explains Bob. "It's been my life for so long, I'm not sure what my life would be without it. I've built it from scratch, you know. And while Jimmy is a great worker and the natural one to hand down the business to, I'm not convinced he can handle managing the whole thing."

Sue then speaks for the first time. "And Bob isn't getting any younger. I had hoped our Golden Years would be filled with time with our grandchildren, some travel, and doing more things together. Bob is so concerned about the business at this point, he's not available for any of

these things, really.”

Fred then turns to Bob. “Bob, if your business concerns were addressed to your satisfaction, what would your other goals be?”

Bob is startled by a question he had given little thought to at any point in his life. His first thoughts upon waking in the morning and his last thoughts before he falls to sleep at night are about Baker Pumps. And while his favorite pastime is fishing in the Keys, he has been so oriented to the success of his business that he has given little thought to his personal future apart from the business.

As Bob gropes for an answer, Fred waits a moment and then responds to Bob’s silence. “Let me state that question another way, Bob. Others I’ve worked with in your situation have figured out a number of priorities and goals, so let me see how theirs stack up against yours.”

Hesitant to begin, Bob is relieved at Fred’s intervention. Fred saw that Bob had reached a block in his thinking and he needed to step in to keep the discussion moving. Fred continues, “Most couples in your situation are thinking about retirement. Today, this doesn’t mean sitting in a rocking chair on the front porch, though it may mean sitting on the veranda of a nice resort every so often. Their first consideration is bound to be financial security—having enough money to see them through the coming years, meaning both sufficient annual income to live comfortably and reserves to handle possible illness or disability. Does this sound like a top priority for you?”

Bob and Sue nod. “Yes,” they say in unison.

Fred continues, “Most couples also have some ideas about what they would like their retirement to consist of, whether or not they have discussed it at all. So tell me, what is your idea of ‘retirement’.”

Bob responds first. “I guess I’ve always thought about not having the headaches of managing the business. I love this darn work, but it’s wearing on me. And while I’m at work I find myself thinking more and more about fishing at our home in the Keys.”

Sue responds too. “We love that home, and it’s so nice having the family there. We’ve always said we never spend enough time there. And the grandchildren love it so.”

“It’s also a special piece of nature you don’t find anymore,” Bob adds nostalgically. “We love the fishing and the wildlife. It was the greatest investment my dad ever made on a grocer’s income. “It’s my only getaway. If I couldn’t count on our home in the Keys, I don’t know what I’d do. And having time there with our grandchildren on a weekend makes me think twice about coming back to work on Monday morning, believe you me.”

The estate-planning process has now begun. Fred has successfully engaged the Bakers into talking about what is most important to them and their future. Notice that he has spent most of his time listening to them, asking a few well-placed questions, and has focused on what their

perceived needs are. He has not used any professional jargon or legalese, yet he and the Bakers are quickly and smoothly launched into the estate-planning process. Fred continues his line of questions based on the Bakers self-identified interests.

“It sounds like your family really means a lot to you. What thought have you given to passing along your estate to them?”

## **Family Ambiguities**

Bob responds first. “We’ve always pretty much assumed that the kids will get what we have. Jimmy works with me day in and out at the business, and by rights he deserves to have the whole thing someday. But that wouldn’t be fair to the other kids, and actually I’m not so sure Jimmy can handle a \$6.0 million business.” Then Bob pauses.

Sue waits a moment until the silence becomes awkward. Then she speaks, but with great hesitation. “Fred, Bob should mention our oldest child, Joe. We’re not close to him and his wife, and this has always been a big disappointment—to me for sure . . .and I think to Bob more than he would admit. Joe lives far away and doesn’t come often. He and his wife have a baby we haven’t even met. And Joe has always claimed he is ‘too busy’ for our family get-togethers in the Keys. I’m not sure how Bob feels about giving anything at all to Joe, but he is our son and should get something. It’s as if he’s not even a part of our family anymore.”

Then there is a long, uncomfortable pause in the conversation. Fred is uncertain as to its meaning, yet rather than push the conversation, he waits for the Bakers to continue. Reluctantly, Bob begins in a quiet voice. “Also, Fred, our Jane is a love, and we’re very close to her and her children. Sue might not want me to say this, but Jane’s husband brings a lot of baggage to the family.” Always the master of understating personal issues, Bob continues. “She can never be sure to count on him, so I don’t want him involved in the future of Baker Pumps. More problems I don’t need.”

Sensing a very difficult issue, Fred responds by supporting both Sue and Bob. “Well, every family has its ups and downs. And material blessings do not guarantee total happiness as we all know. Tell me first about your concerns about giving something to Joe, and then some more about Jane.”

Bob responds quickly. “Joe has turned his back on the family. Why?—I haven’t the foggiest idea! But why should we give him anything if he doesn’t want to be part of the family?”

Fred notes the intensity of Bob’s response. Yet from his experience he knows that when families consider what to do with the assets they have accumulated, they also must deal with the lifetime relationships and their feelings about these relationships which have built up over time.

Fred responds to Bob’s feelings. “Bob and Sue, every family—every family—I’ve worked with has something going on with one or more of their family members. Some people design their entire estate plans to punish wayward family members. And I mean not just to exclude



them, but actually to punish them by giving assets to others instead, or by giving them only a token bequest. While this may be a tempting course for you, I suggest you consider its consequences very carefully. I don't believe you are vengeful people, but I do understand this is a delicate relationship with Joe, and you're not sure what to do. My experience is that problems like you are sharing with Joe are solvable, even though at first glance you may have no idea how, or even where to begin. What more can you tell me about Jane?"

After another lengthy pause, Sue begins to speak, a tear coming from the corner of her eye. "This is hard to talk about to a stranger, Fred, but we just don't know what to do. Jane's husband has never amounted to anything. Why she married him we have no idea. At least she and the children live in town and we get to see them often. But . . .," Sue hesitates, groping for words, "we think the marriage is very painful to her, and to the kids, too. At family parties he gets too drunk to drive, and she has to take the wheel. She is very proud and would never admit to having a problem. But we think she's in trouble, and we don't know how to help."

"I appreciate your candor in sharing with me," Fred responds. "I know it isn't easy talking about family problems, especially about your own children. I do know someone who helps families facing your challenges. His name is Bill Smith, and his communications firm helps families solve all kinds of problems, even if at first they seem insurmountable. He's helped a number of my clients. Why don't we come back to these issues—as difficult as they are for you—a bit later. We will list these relationships as points to consider and their possible options later this morning and now keep talking about any other goals you may have."

Bob and Sue have been uncomfortable for a long time about Jane's situation and with Joe's alienation from their family. Because they did not know what to do, or where to turn, it has been easiest to just set their feelings aside. Now that they hear there may be a way to solve these dilemmas, however, they are more willing to talk about them. They are more than a bit curious about how Fred Scott's associate might help.

## **The Notion of Philanthropy**

"Let's change direction a moment to a new area," says Fred. "You have been blessed with financial success and in spite of the problems with Joe and Jane, you have some very satisfying relationships with friends in this community. What thought have you given to leaving a legacy—a philanthropic gift to your favorite charity?"

Bob and Sue had never really discussed much about their estate beyond the business and family prompting Sue to ask why Fred has raised the issue of philanthropy. "When couples with significant assets such as yours are considering their estate plans, they often reflect on the reasons for their good fortune and the people and institutions who have been instrumental in their success. Some are grateful for the education they received that launched them on a successful career. Others appreciate the medical care a doctor or hospital has given, allowing them the enjoyment of their retirement years. Others want to make a spiritual contribution, whether a tithe

to their church or a gift to a special religious organization. Many have been touched by a charity at some point in their lives and now, with means at their disposal, want to say ‘thank you’ in a tangible way.”

Bob and Sue look at one another for a moment. “Well, my dad might not be here were it not for the Goodall Clinic,” Bob observes.

“Dr. Henderson saved his life,” Sue adds. “We’ve often mentioned how grateful we are to Dr. Henderson and the Clinic, but we’ve never thought about making a gift to them. Aren’t they a business just like any other?”

“Actually, they are a non-profit organization,” Fred replies. “Some of my clients have made gifts to them in the past, so I know they are a registered tax-exempt organization. They do more than just take care of patients too. They conduct heart and cancer research, for instance, which people are surprised to learn. It’s one of their strengths. You might want to think about them as a beneficiary. And perhaps your college or church too. While you may not have given this area much thought to date, the reason I bring this up is that there can be significant tax benefits for charitable gifts in your estate plan. Just as important for some couples, however, is the sense of satisfaction for ‘giving back’ to a charity whose mission is close to their hearts. On some occasions, couples have decided to create a private foundation to carry on values that are part of their own family identity, such as college scholarships for deserving children, health-care research in a medical area of special interest to the family, or even promoting certain social values such as neighborhood improvement or community benefits. Why don’t you give this area some thought, and we can come back to it later.”

Fred continues, “Are there other areas of concern you have as you look to your future? I have listed so far (Fred reads aloud):

### **Summary of Goals**

- having a stream of income that will maintain and protect both of you as long as you live;
- dealing with the management and control of Baker Pumps;
- deciding how to assign your estate among your children and perhaps grandchildren;
- planning your estate to minimize taxes;
- and perhaps deciding what legacy to leave not only to your family but also to charity and your community.”

Bob and Sue appreciate Fred’s summary of what has been a brief but emotion-packed discussion. It is intense for the Bakers because of what is at stake for them—the future of their

business, their own retirement future, and the well-being of their children whom they love very much; the unresolved family difficulties with their children Jane and Joe; and their concern about Jimmy's capability of managing their largest asset, Baker Pumps. And hovering in the background of the discussion is the Baker's realization that they will not live forever. The control they now have over their lives and assets will eventually need to be transferred into capable hands. They agree with Fred's summary.

## **The Search for Solutions**

After identifying the family's goals, Fred is now ready to move into a problem-solving mode. He informs the Bakers that before he can design a plan for them that will stand the test of time, the discussion needs to turn to the Bakers' business-succession concerns.

"Since the centerpiece of your estate is Baker Pumps, let's talk about its future. Tell me your thoughts about the succession of your business."

"Well, as I said," Bob explains, "My C.P.A. thinks it's time to take a big growth step. But that's a big move, and one I'm not sure I want to take. I want to take a step, but back, not forward. And no matter what I do, I'm not sure Jimmy can handle all the responsibility of such a big business."

"Have you talked to him about it?" Fred queries. "Well, somewhat, on and off," Bob responds. "But I haven't sat down and told him my concerns, so we really haven't come to any conclusion. And it's hard for me to come out and say to my son I don't think he's the man for the job."

"Give me your assessment of Jimmy, both of you," Fred asks. "And be sure to note all his strengths and resources. Let's see where this takes us."

"He's a good kid," Bob begins. "We get along well, so I have taught him a lot. He's a hard worker, so he's quite motivated to be successful. He's great with people, and the customers love him, but it takes more than that to keep things humming. If he had to fire someone, I don't think he would be up to it. His people skills could be useful there, but I'd have to see. And he's not exactly an Einstein with numbers either."

"You know, Fred," Bob pauses, "still, if I didn't have him at my side at Baker Pumps, I'm not sure what I'd do. He's always there to count on, and I can trust him. That means a lot."

"So," Fred summarizes, "you have a good working relationship with him, he's motivated to succeed and do what it takes to succeed, he's a strong ally, and he has strong and dependable people skills. Those sound like solid assets, although you wonder if he could fire someone. What do you picture happening if he were in charge, Bob?"

"Well, that's a tough one," Bob ponders. "I've got solid engineers who have been with me a long time. Jimmy understands the manufacturing well enough. And he's great at sales and

always coming up with new ideas for advertising. I guess, my concern is about handling responsibility. He does everything I ask him to do and he's a hard worker, but I just don't know."

"It sounds to me as if he has many of the qualities to be an excellent manager," Fred observes. "What else could you ask him to do that he'd do willingly? It sounds like he just hasn't had the opportunity to be accountable."

There is a moment of silence at this point. Fred's casual observation has hit the nail on the head. Bob's hesitation in the conversation reflects his concern about Jim's ability to handle responsibility. Bob concedes he doesn't have confidence in Jim's ability to handle responsibility because he has never had a major responsibility handed to him. This would require that Bob take a significant risk with a multi-million dollar asset. But even more difficult, it would mean that Bob would have to trust his son as his equal—a huge step and one Bob has never taken with his company his entire life.

There is another long pause in the conversation, and then Sue interjects. "You know, honey, Jimmy has always done his best for you. And you haven't exactly given him the chance to show what he can do. Remember when we took those two weeks in the Caribbean and left things for Jimmy to run. Jimmy handled everything extremely well, but when we got back you yelled at him about that invoice that was lost under a stack of bills. You never gave him credit for running the place or thanked him, for that matter. And you fretted about work every day of the vacation."

Rather than dismiss Sue's comments as those of an overprotective mother, Fred pays attention to her observations. He understands entrepreneurs like Bob. He knows how important the tight reins of management are to the entrepreneur, because there are so many things over which the entrepreneur does not have control—competitor challenges, market forces, customer complaints, employee dissatisfaction, government regulations, and tax policy among them. And Fred knows that every successful entrepreneur worth his or her salt is successful because of ambition, drive, and perfectionism—virtues he prefers to see in others who will have responsibility for his company.

"Oh, Sue," retorts Bob, "you know I have every faith in Jimmy. He's a good kid."

But here Fred interjects. "Yes, I'm sure Jim is a good person and a fine son. But, that alone won't qualify him to run your business or guarantee success. Bob, in addition to being a good person yourself, you know the blood, sweat, and tears you have given to make Baker Pumps a success. What would Jim have to do to show you that you could have confidence in his abilities?"

Fred has deftly framed Bob's dilemma. He has already noted and highlighted Jim's strengths. Fred is attempting to ascertain Jim's qualifications based on what Bob himself has identified as Jim's resources and how they will fit the task of taking over Baker Pumps. At the same time Fred affirms Bob's success and all it has taken to achieve it.

"Imagine for a moment you and Sue won a three-month cruise around the world. What would be the steps Jim would have to take to assure you that he would be successful when left in

charge?” Fred queries.

“Why I can’t imagine that,” replies Bob.

“Then how would you really know whether Jim can handle the job alone?” asks Fred. Bob sits in silence.

Fred continues. “You know, Bob, you have taken enormous risks in building Baker Pumps. But they have been staked in your confidence in yourself, in your belief that you can overcome all obstacles in any shape or form. Where did you get that confidence? How did you develop it? It doesn’t come overnight.”

This question really hits home with Bob. He responds with feeling. “I started working when I was 14. I swept floors and even handled the cash register at my Dad’s grocery store. I stocked shelves after school; and when other kids were playing ball, I was learning to wait on customers.”

“So you learned it by taking responsibility, and that built your confidence in yourself and your abilities. Were your abilities ever tested?”

“Absolutely,” Bob replies. “Once when I was 16, I ran the delivery truck into a telephone pole. When I was 17, I gave someone credit for \$20.00 of groceries, and they never showed up again. My Dad yelled at me for a week for each of those.”

“Yet, I’ll bet your Dad continued to trust you—he had confidence in you and your abilities?”

“Why, as a matter of fact, he did!” exclaims Bob. “How do you know that?”

“From my clients I’ve learned that two traits of successful entrepreneurs are self-confidence and perseverance. They have the confidence in themselves to persevere and to succeed. And where have they learned that virtue?—usually from a parent who persevered with them growing up as they learned the family trade or business. How do you think you could generate that same confidence in Jim?” Fred inquires.

Fred is surprised by Bob’s sudden laugh. “You know, Fred,” Bob replies, “I’m really not sure. I see the parallel between what my Dad did for me and what I could do for Jim, but I’m just not sure how to do that.”

“How did your Dad demonstrate his commitment to you?” Fred responds. “He let me know in ways both large and small that I could do anything I put my mind to,” Bob reflects, “and he truly showed me what it took to succeed at the family grocery business. I never wanted to be a grocer like him, but I knew I wanted to do more, to create something special, and to be someone. I guess I got those ideas from him.”

“Or perhaps he created an environment in which you could actualize your potential,” suggests Fred. “Is that what you’re not sure about with Jim, just how to help him be successful?”

“You’ve right, Fred, absolutely right!” Bob says with sudden insight. “I do want Jim to succeed, but not sure how to go about doing it.”

“Well, that’s a great awareness to work with, Bob. I think you’ve already taken a big step on that path. Let’s jot this down as a point to consider as part of your management-succession solution.”

Fred has persevered enough with Bob to help him through a sticking point in his agenda with his son. At the same time, Fred doesn’t want to get bogged down with the point. The goal for today, after all, is to create a solution-oriented framework for Bob and Sue as they consider their future. Fred has accomplished this in the relationship with Bob and Jim, and it is time to keep the conversation moving forward. Fred notes on his legal pad Jim’s assets, which Bob has identified—“work together . . .teachable . . . motivated . . .dependable . . .good with people . . .,” and adds as well, “how can Bob show his support?”

Moving on, Fred comments, “I assume from what you’ve said about Joe and Jane, that neither of them is a candidate for running Baker Pumps. I understand if Jane is preoccupied with family problems, you’re not sure she’s in any position to help with the family business. Is that right?”

Bob and Sue nod in agreement. “Then that brings us to Joe,” Fred suggests. “Tell me some more about your relationship with him.”

Before Bob can respond, Sue jumps in. “Joe—to be honest—is a sore point. We just don’t understand him. It’s not as though we argue a lot. He and his wife are pleasant to us, but we seldom see them. There’s an occasional phone call or letter, but we have nothing much in common. It’s such a strange contrast to our other two children.”

Just by Sue’s initiation of discussion in this area, Fred assumes Sue feels it’s easier for her than Bob to discuss Joe’s alienation. Fred has found that sometimes mothers can be the emotional thermometers of a family. He surmises that the Bakers’ problem with Joe is an emotional hot spot, particularly for Bob. From past discussions with Bill Smith whose expertise as a family communications specialist Fred respects, Fred has learned that families are just like small businesses in which each part is related to every other part. Therefore, Joe’s alienation could significantly affect the estate-planning process. And while the difficulties between Joe and his parents are not entirely clear to him, Fred assumes Bill Smith will be able to shed some light on this area for the Bakers.

Because Fred is concerned about a solid business-succession plan, he explores the relationship with Joe a bit more. “Has Joe ever expressed an interest in the business?” Fred asks.

“Never, ever,” responds Bob. “At the family dinner table when the kids were younger, Sue and I would discuss how my day went, the ups and downs of the company, and Jane and Jimmy might ask questions, or in their own way even try to be helpful, but no, not Joe. Never.”

“And it’s more than that,” adds Sue. “As an adult he always pursued his own interests, ‘my

own thing,' he would always say. And while the other kids would come to us for advice, or for ideas about college and their careers, Joe only did when he needed money for his graduate degree. Jane and Jimmy both attended our alma mater, the University of the Southeast, but would Joe consider attending? Not a chance. He went out of state. To his credit he got an academic scholarship to a fine private school, but he always did things differently from the rest of the Bakers."

"So your concerns are about connecting more closely with Joe and his family, not just about his place in the estate?" Fred queries.

"It's just so frustrating," says Sue. "Bob and I worry about Joe often, but we never have come to a satisfactory solution."

## **The Family Retreat Option**

Having listened carefully to the Bakers for the better part of an hour, Fred Scott knows they are near a stopping point. From his experience drafting estate plans for well-to-do families, he also knows that the Bakers' problems are not unique. Yet, because the family business and its fate will be the centerpiece of their estate plan, and because of the unique set of relationships that occur in families with small businesses, he knows that their relationships are going to have to be addressed if a successful estate plan can be drafted. He has seen too many failures in which unaddressed feelings and lingering resentments have sabotaged estate plans—plans that would otherwise guide the successful transition of the family business and the current generation into their golden years. And he has witnessed faulty or naive assessments by parents of their own children—unaccompanied by acknowledgment of the children's inherent resources—assessments that ultimately led to the unnecessary dissolution of the parents' fondest dreams.

"Given your desire to more closely connect with Joe and determine his place in the estate plan, your concerns for Jane's place in the estate plan given her difficulties at home, and a plan to guarantee Jim's success at the helm of Baker Pumps based on the strengths and abilities you've mentioned, we need some more thought to best ensure the future of the company, and of course the best future for you two as well. Families in your situation, I have found, benefit most from a family conference on their pending estate plan. You are building the foundation for your future in this plan, so nothing can be more important than having the foundation firm and secure. I recommend," Fred concludes, "that you invite the kids to a meeting with me present in order to discuss the concerns you've shared with me."

"You mean sit down and talk with them like we're talking now?" says Bob a bit startled.

"Yes, exactly," replies Fred. "I would be there, and I would invite my colleague, Bill Smith, whose expertise in helping families achieve satisfying succession plans can really be helpful here. He and I have had conferences with many families like yours."

"But this is rather personal, Fred," responds Bob. "A family conference would be hard

enough for Sue and me with the kids, but to have a stranger there—I mean we like you and everything. And then someone else too. I don't know.”

Bob's reservations are familiar to Fred. But he replies, “Bob, how much is at stake in making a successful transition for Baker Pumps?”

“Well, EVERYTHING, of course,” Bob responds.

“As the businessman that you are, would you leave any stone unturned to ensure the success of a new line of Baker Pumps?”

“Well, of course, I'd make darn sure every base is covered.”

Fred goes on. “That's all I'm saying, Bob. Let's get together and uncover all the resources available. No successful entrepreneur would think of making decisions before he knows all the resources he has to work with. We are talking about your and Sue's entire future. You have worked decades to build Baker Pumps into a great success story. But the story isn't over. Now you're at a critical point in writing your last chapter to determine how your story turns out and how the sequel begins. You're facing the risk of the unknown, yet you've done that many times before and done so successfully. It's just that the 'unknown' here is a bit more unfamiliar to you. As you have in the past, I'm suggesting you call in advisors.”

“I realize family relationships are a delicate matter,” Fred continues, “but what better way to assess your children's abilities to handle major business and financial issues than to see them in action discussing the future of Baker Pumps? You will be able to see what business acumen Jim has. You could use it to reassess your relationship with Joe before you make a major decision about him and his family, and you can see how Jane functions concerning business decisions that have nothing directly to do with her marriage. Bill Smith and I have worked with families like yours before, and we've found conferences to be extremely helpful to both the parents and the adult children, offering a way to include everyone's voice in resolving any concerns. I recommend that you ask Jane, Joe, and Jim to come with their spouses to your home in the Keys for a weekend, but without the grandchildren. On Saturday, Bill and I would arrive for two days to guide you all through the family discussion process. You and Sue would speak with Bill ahead of time, and he will tell you about structuring the day and discuss what he has in mind. You and your children and your grandchildren have an enormous stake in the future of Baker Pumps, certainly worthy of the time. We'll call it the Baker Succession-Planning Retreat.”

Bob and Sue look at one another, each more startled than the other. “I've heard about these family retreats,” says Bob. “But I thought they were just a strange 'touchy-feely' thing or just an excuse for a vacation.”

“Well,” responds Fred, “the focus is the future of Baker Pumps and the resources that will keep it thriving. It will be a family problem-solving session much like our conversation today. We've covered a lot of territory today among us, but we're stuck on three points in the succession plan that correspond to each of your children—Jim's role in the business, Joe's place in the estate plan determined by his relationship with the family, and Jane's role in the estate plan



and any impact her marital difficulties may have on it. If you make a decision about these issues today, it will be premature and most likely a failure.”

“I like the idea of making an assessment of the kids’ abilities,” Bob responds. “Actually that’s a great idea.”

“I’m sorry, but I still am not clear how a family will retreat help,” Sue continues.

“Surprising as it may seem,” Fred continues, “Jim, Joe, and Jane can be helpful in solving the business problems you’re facing as you discuss the expectations, hopes, concerns, and difficulties in your family. You two have always had the burden of decision making in the family. But now your children are adults and you are ready to make difficult and important decisions about your business. You have given them fine educations and they are responsible adults, even though—like all families—you don’t agree on everything. Your children have lived through the struggles and successes of Baker Pumps. Their upbringing has been as affected by the business as much as your lives have been. And they have both financial and emotional stakes in its future. They, no doubt, will have ideas and feelings about what you decide to do with the business. You may be surprised how helpful their input may be.”

“I do see how they’ve been affected by growing up with Baker Pumps, almost as if the company is our fourth child,” Sue observes. “And I remember how some of our dinner conversations about the company problems really upset the kids. Remember how Joe left the table and slammed the door of his bedroom when he was 12, Bob? He was so mad when you had to fire Ed Jones, the mechanic he liked so much and who was teaching him about pumps. I thought he’d never get over that one.”

“I had forgotten all about that,” Bob reflects.

Sensing a connection Fred asks, “I wonder if he still remembers it. Why do you think he was so upset when Ed was fired?”

“He never mentioned it,” Sue says.

“Did he ever go back to the plant and learn more about pumps?” Fred persists.

“Come to think of it,” Bob observes, “he never did.”

“I remember now,” Sue says. “He started a science project right afterward. Remember dear, he won the blue ribbon at the state science fair?”

“Hmmm,” Bob responds. “You don’t think there’s any connection there, do you Fred?”

“It certainly makes sense that Joe could have made some decision about the business at that point. It’s a good example of how the family business can affect the kids,” Fred observes. “The family business is like a member of the family, sometimes demanding and frustrating, sometimes a joy, but always present. That’s why involving the whole family in a retreat setting can be so helpful in making the best plan for the future of the family business.”

“And Jane would always go to her room and play her rock and roll music whenever we had family arguments,” Sue adds. “She would just disappear. Jimmy was always the one who tried to make things OK. Are you saying, Fred, that these orientations still affect our kids today in adulthood?”

“In some fashion, yes,” Fred replies. “I’m not a psychologist, but I do know children’s attitudes toward the family business are formed at a young age, are reinforced as they grow, and influence their own career and family decisions as adults. It would be interesting to hear what Joe and Jane have to say about that, how it affected their careers and decisions and ideas about the company.”

“You make your case well,” Bob replies after a moment. “But it would take a lot to get Joe and his wife to the Keys. I just don’t know. And Jane’s husband can be a handful. It could get pretty touchy.”

“To Joe, you can explain that’s it’s to help you and Sue decide about the family business and any role he may play in it,” says Fred. “He grew up with it, he has a stake in its future. To Jane you can explain that you two must make decisions about her inheritance and her children’s. And to both you can say that while you and Sue will make the ultimate decision about the future of Baker Pumps and the shape of your estate plan, it will be helpful to have their input. It will only be for a day or two, but it is critical to their future and to the future of their children—to the future of the entire Baker family. Tell them all that the goal is the estate plan and their roles in it.”

“Do you think Joe would go for it, Sue?” Bob asks. “I think if we both call and ask him, he might,” says Sue. “It isn’t just family time that you know Joe has so much trouble with. We’ll be discussing the business and his stake in it, and that will be our agenda. Is that right, Fred?”

“Exactly, Sue. Bill and I will prepare an agenda to follow for the day which everyone will have ahead of time. And most importantly, we will clearly define the goals so everything will be on the table for everyone to see. Why don’t you two plan a weekend and let the kids know what you want to achieve, and Bill and I will set up the rest.”

“Well, I guess it’s worth a shot,” Bob replies warily. “I know these problems won’t solve themselves. Maybe Joe will come; I think Jane will in spite of everything. And I’ve got too much invested in Baker Pumps to make a plan that I know won’t work. I’m not enthusiastic about this family retreat thing, but I’m willing to give it a try.”

Fred’s experience tells him that this is as positive a response as he could hope for from the founder of the family business and patriarch of the family, a man committed to the best for his business and family. Fred knows that this is a big step for Bob and Sue, but one which has the potential to pay them enormous dividends for their succession plan. He doesn’t expect them to be totally convinced, but he knows that he and his colleague, Bill Smith, have a core of commitment with which to work on the family succession-planning retreat.

## **Preliminary Retreat Considerations**

“That’s great, Bob,” replies Fred. “In my eyes it will be well worth the time and effort given all that’s involved in making a solid estate plan.”

“So what’s the retreat going to cost?” Fred asks.

“It’s the same fee structure that I have. Bill also charges \$350 an hour for his time. A retreat for one to two days would be billed on a straight hourly basis.”

Bob quickly adds up the hours in his head, and the cost, but concludes his concern by saying, “I hope it’s worth it.”

“The proof is in the pudding, as they say,” Fred responds. “If you have concerns about the cost, why don’t you talk a bit more with Bill Smith about how retreats have worked for other families. “While you are making arrangements for the retreat, you have some homework to do as well—getting together some documents and materials. Reviewing them may prompt some ideas to discuss at the retreat.”

At this point, Fred gives Bob and Sue the Client Information Sheet. As they page through the various schedules on the sheet, they begin thinking about their particular assets and what retirement purpose each might serve.

Fred also notes Bob’s and Sue’s initial reactions to the Client Information Sheet. Bob mentions that he isn’t sure what to do with the vacation home in the Keys, with his I.R.A., or with his brokerage account. Fred takes the occasion to continue their discussion a bit further.

Fred mentions at this point that so far they have been discussing the Bakers’ mutual goals and objectives. Fred makes it very clear to Bob and Sue, however, that they each need to know whom he represents in the estate-planning process. It is possible that he can represent both Bob and Sue if their goals and objectives are common and if there would be no conflict of interest. Bob feels that he and Sue have done everything together and there are no conflicts or disagreements in their marriage. Sue nods her head in agreement. They are willing to sign whatever papers are necessary to authorize Fred to represent both of them. This means that Fred is free to fully disclose any and all information with which he comes into contact with no secrets held from either spouse.

Fred has learned from painful experience what can happen when one spouse acts without the knowledge or consent of the other. In this case the relationship Bob and Sue built over their 40 years of marriage by learning to tolerate and resolve differences bodes well for building a solid estate plan. It is this plan that will structure their financial—and in many ways, emotional—comfort as they prepare for the last stages of their lives together.

Fred is aware, of course, that Bob and Sue may have different priorities, and they may have different assessments of the children and the role each one plays in the family. Sue seems more interested in resolving family relationships and reunifying the family. Bob seems more interested

in directing the decisions about the future of the company. These priorities are not necessarily incompatible, and Fred can work with these differences. From an estate-planning perspective, however, the ultimate plan must have both Bob's and Sue's endorsement.

Bob has a long-standing relationship with his financial planner, Susan Jones. He asks Fred what part she would have in the estate-planning process and also whether or not his C.P.A. would have some role to play. Fred explains that the estate-planning process will be a team effort involving his business advisors—including his financial planner, his C.P.A., and perhaps a trust officer to arrange the trust opportunities that Fred foresees with the Baker estate. Others may be involved as well, depending on which direction Bob and Sue choose to take, such as a gifts planning officer from their favorite charity, and of course, Bill Smith the family communications specialist who will work with them on the family retreat.

Fred then presents Bob with several other documents for them to read over before their next office conference. These documents explain in layman's terms some of the basic concepts underlying estate planning. All the terminology can be a bit confusing at first, so Fred's materials include explanations of the unlimited marital deduction, the unified credit, annual exclusion gifts, and the generation-skipping tax.

Reviewing the list of documents, Bob raises the question of the future of the estate tax. He asks Fred why he and Sue even need to worry about all these details.

Fred explains that the current estate tax exemption, gift tax exemption, and GST exemption, are all \$5.0 million each. However, in the year 2013, all three exemptions revert back to \$1.0 million unless congress takes further action.

Bob and Sue listen with a look of hesitation on their faces. Fred assures them that in this uncertain climate for planning, he believes the best route to take is to create a plan based on the current situation, and then to monitor the plan with ongoing developments. Adding that the retreat will involve detailed discussion about their estate, he also states that many of the issues facing the Bakers are not tax-related, such as issues relating to who the business successor might be, how to treat all of the children fairly regardless of who gets the business, the need for protective trusts for certain beneficiaries, retirement issues for Bob and Sue, and some charitable issues.

Before Bob and Sue get sidetracked on these concerns, Fred returns to the list of documents he gave to them. The documents explain to Bob and his wife that any property transferred to either spouse by the other, either during lifetime or at death, will generally qualify for the unlimited marital deduction and thus no tax. Each spouse also has an exemption that will allow each one of them, either during lifetime or at death, to transfer substantial assets to other family members with no federal gift or estate tax.

Bob acknowledges that it is a good idea to have all this in writing as he would have a difficult time remembering everything. He will be able to refer to these documents in the future as various questions arise. Also, Bob mentions that he has heard about the possibility of giving

away annual gifts of \$13,000 but is not certain if this used up any of his exemption. He is also uncertain as to how many people he could give to and how often these gifts could be made. Fred explains that a husband and wife may *each* give up to \$13,000 (adjusted for inflation) ‘of a present interest’ to as many individuals as they choose. None of these annual gifts of \$13,000 reduces either of their exemptions. Fred also explains that in addition to these annual gifts Bob and Sue can also make gifts to pay any person’s (including grandchildren’s) tuition and medical expenses provided that the checks are written directly to the institution or to the provider of medical care.

Fred also explains to Bob that he knows he has a very large rollover I.R.A. It will be subject to not only estate tax but also income tax when the money is withdrawn. In addition, there are various penalty taxes involved for taking money out too early, taking money out too late, and taking out too little money. Part of the planning process will be to figure out how and when Bob and Sue should take out their funds from the I.R.A. Bob and Sue have worked very hard over the years to acquire all of their many assets, and it will be quite disconcerting to them to realize how significant the income, estate, and gift taxes can be.

Fred acknowledges that Bob and Sue are very fond of their grandchildren and would like as part of the process to make gifts to their grandchildren. Fred also mentions that there are many planning opportunities to do generation-skipping to avoid estate taxes at their children’s level and that there are also opportunities to make sizable gifts to a charity that will generate both income and estate-tax savings.

While Bob and Sue have been very supportive of their local church, Bob expresses that they plan to make only a small gift to their church in their Last Wills and Testaments. Making a gift to the Goodall Clinic is a new idea that intrigues him, but one he wants to think about.

Fred assures Bob that this whole process of estate planning will not be as difficult as it might seem at this point, but that it will take several months to accomplish. Before leaving, Fred presents Bob with another sheet, a list of documents for Bob and Sue to obtain and have delivered to him before the family retreat along with the completed questionnaire. Fred asks that he be provided with the corporate record book for the company, deeds to all real estate, copies of all life insurance policies, copies of their I.R.A. plans and beneficiary designations, and copies of their most recent brokerage statements including I.R.A. statements. Bob indicates that this material will be forthcoming shortly, and that he will be contacting his financial planner and accountant to help with the gathering of the requested information. Fred asks Bob to apprise his advisors of their conversation in anticipation of playing a role in Bob and Sue’s financial, estate, and retirement planning. Fred gives Bob several of his business cards and indicates that any of his advisors should feel free to contact him if they have any questions when they are putting together the basic financial information. He also gives them Bill Smith’s card and gets their approval for Bill to call them.

Bob and Sue leave Fred’s office with a sense of relief. They have taken the step that Bob has avoided for so long—tackling the future of his business and, indeed, of his and Sue’s future. The

process still seems very complicated, but Fred seems to know what he is talking about. Bob has confidence in his attorney for two reasons. For one, Fred seems to understand what it's like to be in Bob's shoes. And second, he's gone through this process before with others and seems a trustworthy guide. Sue has confidence in Fred as well. She's pleased he has taken her into account as a full partner in the planning process. She also feels reassured that he understands her feelings and concerns about her family, and she's surprised to see he understands how the business has affected her children as they have grown up. Furthermore, he is not turned off by their revelation of their family problems, and he has even taken a positive perspective on solving them. Bob and Sue's confidence in Fred enables him to take the next step, making arrangements for the family retreat with his colleague, Bill Smith.

## **Reflections**

1. Fred establishes rapport with Bob and Sue right away. First of all, he recognizes and immediately acknowledges that just coming to his office is a challenging step for Bob. Second, he acknowledges his new relationship with Sue and the unique perspective she has in creating the estate plan.

2. Because so much is at stake for them, the Bakers listen to their attorney's advice with a cautious ear. How their concerns are responded to is an excellent barometer of this professional relationship. Any initial discomfort Bob and Sue may have quickly evaporates through Fred's warm approach and his nontechnical and jargon-free focus in the first meeting. Fred also emphasizes that they will be involved "together" in developing the plan, channeling any entrepreneurial concerns about control into a positive assessment of the company's needs and the resources available to meet them. Fred also repeatedly references the hard work, loneliness, and struggles Bob has endured on his way to success. This empathy lets Bob know that Fred truly understands what life is like from the entrepreneur's point of view.

3. Fred recognizes that every interview is different, so Sue and Bob's motivation to speak candidly is not necessarily typical of every client. Yet given the opportunity to speak in a supportive, reassuring environment, most couples will be open about their family concerns. The Bakers are naturally hesitant to discuss their family problems in front of strangers. Yet Bob and Sue clearly understand that the Baker family relationships are the foundation on which a solid business-succession plan must be based. Their other alternative—selling the family business—would dramatically change the sense of the Baker legacy so important to Bob and would be seen as an inappropriate choice for this family.

4. Fred knows from experience just how overwhelming the estate-planning process can be for clients going through it for the first time. He acknowledges this and is careful to go step by step through all the initial considerations. At the same time he continually leads them through the recognition of Jim's abilities and the necessary criteria to maintain the success of Baker Pumps.

5. In discussing the family relationships, Fred knows he is out of his area of expertise. Yet

he also knows how unresolved conflicts in family relationships can destroy his estate/succession plan either before he can really get started or even later down the line. Thus he suggests the resources of a trained professional to assist the Bakers in the format of the family retreat. Fred takes a respectful approach, allowing Bob and Sue to decide about their family and the family retreat. By asking open-ended questions, he allows them to indicate their ideas and priorities. By respectfully exploring their responses, he uncovers strengths and abilities and resources that had previously gone unnoticed, and can now be activated to address the company's needs. Yet he is direct in letting them know the importance—especially in a small business family—of family relationships and a goal-oriented format in order to accomplish their estate- and succession-planning goals.

6. The attorney's focus is always on the perceived needs of his clients within the context of the estate plan. He does not interject his own opinions or moral judgments about their family circumstances or financial affairs. He does have professional opinions about which he is clear and direct. These, however, are always related to the reason the Bakers have come to him, which Bob identified in his first sentence—the future of Baker Pumps.

7. The idea of the family retreat is not a new idea in psychology, but it is new to the Bakers. They are receptive to it because it appropriately addresses the nexus of their business and family goals. It can become an integral part of their estate planning while strengthening family ties. Bob and Sue's commitment to their children is critical to their willingness to attend the family retreat and indicative of Fred's skill in communicating all that can be accomplished.

## Chapter 3

### ENGAGING THE FAMILY:

## Family Relationships and Business Succession

### Retreat Preparations and Concerns

In preparation for the family succession-planning retreat, Fred has asked Bill Smith, his colleague specializing in family communications, to contact Bob and Sue. Bill calls to introduce himself and to explain just what the retreat involves and what its goals will be. He reiterates what Fred had said, that the goal of the retreat is to provide a discussion with family members aimed to help Bob and Sue with their decisions about the family business and an estate plan. He goes on to say that the retreat is just that—a business discussion. Knowing about their concerns about their relationship with Joe and about Jane’s marital problems, he assures them that while discussions about family relationships might be aired, the focus of the discussion will be on solutions for Baker Pumps, Inc.

In addition, Bill assures Bob and Sue that they will not be bound by anything discussed at the retreat. The decision about what to do with the company will be totally theirs. However, he said, since all of the children have a shared family history “growing up with the company,” Bob and Sue might find their input quite valuable. He reassures them also that the retreat will not involve counseling or psychotherapy but will be a problem solving session with all the family members involved. Should he discern a need for counseling—for instance marital counseling for Jane and her husband—he will recommend it in a respectful manner at the retreat and provide referrals.

His job, he explains, is to help facilitate the discussion, to help the family stay focused on its purpose of discussing possible solutions for their family business, and to share his experience of how other families have solved some of these same problems.

While the main purpose of the retreat is to help Bob and Sue establish their business- and estate-planning goals, a second purpose is to have the adult children and their spouses agree with the basic framework of the Bakers’ estate plan.

Since Bill is a stranger to Bob and Sue, he provides some background information on himself. He grew up in a family with a small business, and he now runs his own—a consulting firm in the niche of helping families like the Bakers make effective succession decisions with their businesses and their estates. Bill holds a Ph.D. in psychology and has practiced marital and family counseling for many years. A professor at the local university as well, he specializes in



teaching about family relationships and family solutions. Associates in his firm also provide individual, marital, and family counseling.

Bill asks if Bob and Sue have any questions or concerns about arranging the retreat.

Bob's first question involves a confirmation of the cost. "Fred said that you would talk to us about the cost," Bob begins.

"For a retreat facilitated by Fred and me, the cost is \$700 per hour, \$350 for each of us. A day's retreat would be \$6,400. A second day would be another \$6,400."

"That's a lot of money," Bob challenges.

"It depends on what value you receive for that sum," Bill responds. "Fred told me a bit about your goals and the challenges you face in reaching them, particularly in regard to each of your three children."

"That's right," Bob and Sue say in unison.

"Tell me," Bill continues, "if successful, how much would that be worth to you?" asks Bill.

"Why I could never put a value on that," Bob quickly replies.

"Exactly," Bill agrees. "That's why Fred and I charge our professional, hourly fee."

"But how do we know this is going to work?" Bob asks.

"How do you know your next product line, or next marketing campaign will work?" Bill responds.

"Well, I never know for sure, but I decide it's worth the risk."

"What yardstick would you use," Bill says, "to know if a family retreat will be worth the risk?"

"I guess two ways," Bob reflects. "One is its impact on the problem I'm trying to solve. The other is the confidence I have in the resources I'm employing."

"That's a careful and considerate answer, Bob," Bill says with respect. "How does a family retreat with Fred and me measure up on your yardstick? How high an impact do family relationships have on your succession plan?"

"Awfully high, I admit," Bob acknowledges.

"I think so too," Sue agrees.

"That leaves us with the confidence factor," Bill continues forward. "How can you have confidence in Fred and my abilities to conduct this retreat?"

“Fred’s a pretty smart fellow,” Bob acknowledges. “And I’ve always done right relying on his advice. But—to be perfectly frank—we don’t know you, Bill. Your background in family business sounds solid, but this retreat is still a gray area.”

“Then why don’t I give you some names of people to call,” Bill replies, “so you can talk to them about how I’ve helped their families. I can give you their names and numbers before we hang up.”

“That sounds fine with me,” Bob agrees.

“I like that too,” Sue adds.

“Then for now,” Bill moves on, “why don’t we talk a bit more about how the retreat will work. Then you can check out my references and get back to me.”

As the conversation continues, both Bob and Sue agree that Jane and Jim will be happy to participate, but that Joe’s commitment might be hard to get. Bill suggests that they explain the importance of the retreat—that the family business is at a critical point in its history, that the hard work the Bakers have put into Baker Pumps for three decades has borne fruit and now is the time to reap the harvest and secure success by discussing the next step in the business. Bill goes on to say that as a family member Joe will not only be affected by the fate of the business, but also he might wish to have input into that decision.

Bob agrees that this sounds logical enough, but Joe still might have reservations. Bill suggests that probably each family member might have some reservations about the retreat, but upon realizing that the stakes for each family member as well as the stakes for Baker Pumps being so high, it will be very important for *everyone* to attend and have their voice heard. Bill also notes that statistics indicate that only 40% of family businesses make it to the next generation, and Bob and Sue may have strong feelings about Baker Pumps becoming one of those failing statistics.

Bill goes on to say that it is important for the children’s spouses to attend as well. Family businesses affect the well-being of the next generation too. And while the Baker’s children will be most affected by Baker Pumps’ future, their spouses and the grandchildren will be as well. From a business-succession standpoint, only one in three of the 40% making it to the second generation make it to the third generation. That’s less than a 15% chance for Baker Pumps to end up in the Baker family two generations from now. For an entrepreneur considering his legacy, this is a startling statistic, one that underlines the need for planning and discussion immediately. In addition, the Bakers most likely have some idea of passing some of their estate to their grandchildren, and this will be an important topic to explore at the retreat. Considerations of equality are always pertinent too. Grandchildren themselves would not be appropriate for the retreat, Bill goes on to say, because they likely would be a distraction from the discussion.

Hearing this, Bob and Sue agree to call Joe, but with both on the line together to give impetus to the request. As a matter of fact, Bill suggests they make all the calls to the children together as a sign of their agreement on the importance of the retreat.

Sue raises the issue of Jane's relationship with her husband, Jeff. "I'm concerned that everyone in the room will know about their problems and this will hang over any discussion we have about the kids," Sue offers.

"I appreciate your concern," Bill responds. "You do not need to directly make reference to their problems at the retreat since it is really an information-gathering session to help you make your subsequent decisions. You likely have worries that Jeff may not be able to provide for Jane and your grandchildren's financial security. The retreat may serve as an impetus for them to think about that since we will be discussing how to plan for the future. Should issues of Jeff and Jane's marital relationship come out in the open directly, my job will be to identify that as a separate issue, important to be sure, but one which should be addressed outside the retreat setting."

"It sounds pretty touchy," Bob observes. "I'm not sure this will work out, even with your professional expertise."

"Issues of marital conflict and chemical dependency are much more common than most people think," Bill responds. "But these are not to be the focus of the retreat. Personal problems are best handled in a therapy session, not in a business discussion."

"You should also know," Bill says reassuringly, "that every family has the resources for strength and reconciliation that—given the proper impetus—can surprise the most hardened observer. Jane is your daughter, and Jeff is your son-in-law. They deserve a chance to be respected as important and valued members of the family with no premature judgments about their relationship. I'm sure you're concerned about the grandchildren, but they may be more resilient than you imagine. A solution-oriented approach will be your best resource in supporting Jane and Jeff, but also in ensuring that Joe and his wife feel welcomed as well."

Bob and Sue take a deep breath together and agree to proceed. They will call "the kids and the spouses" and invite them to the Baker Family Succession-Planning Retreat.

Separately, Bill Smith and Fred Scott meet to plan the Baker retreat. They have facilitated a number of retreats together before, so they have a good idea of what their professional goals will be. Since Fred has the existing relationship with the family, he will speak first, introducing both himself and Bill. Fred will speak about the critical point Baker Pumps is in its history and the importance of the retreat's discussion for its future. Bill will talk about how unique small-business families are and how each family member in turn affects and is affected by their indirect relationships with this odd "member" of the family—the business.

They agree that Fred will generally set the agenda for the discussion (the content) and that Bill will be involved in promoting useful, inclusive communications by all family members (the process). Both understand that the goal of the retreat is to help Bob and Sue with their decision and that to be successful the discussion will always have to point in that direction.

They jot down the agenda, subject to confirmation with Bob and Sue, which will be sent to all participants ahead of time. The purpose of the pre-published agenda is to communicate three things: (1) the seriousness of purpose, (2) the limits of the discussion, identifying just what will be talked about (very specific topics) and by omission what will not be talked about (anything else such as personal agendas or blame), and (3) a positive, solution-oriented structure for the time spent together. Bill keys in the following agenda on his laptop computer.

### ***Baker Succession-Planning Retreat***

**Goal:** To help Bob and Sue do business succession and estate planning in order to ensure their retirement goals.

#### **Agenda**

1. Introduction
  - a. Business Succession-Planning Fred Scott
  - b. Growing Up with the Family Business Bill Smith
2. Options for Baker Pumps Succession Everyone
3. Estate Planning for Three Generations Everyone
4. Summary and items for follow-up Fred and Bill

### **Setting Parameters for the Retreat**

A week later, Bill calls Bob and Sue to see how their telephone calls to the children have gone. To Bob and Sue's surprise, all three of the children were willing to come with their spouses. While the children each had many questions, they all had an interest in the future of Baker Pumps. All were pleased that their input was being solicited by their parents. Bob and Sue now look forward to the retreat, hoping that this will be a big help in getting their business-succession and estate plan together.

Several weeks later, two generations of Bakers gather at Bob and Sue's vacation home in the Florida Keys. The setting is a relaxed and enjoyable one, and all make themselves available for Saturday and Sunday with no distractions from cellular phones.

Joe and his wife surprisingly, have come in response to the call from Bob and Sue. His parents' acknowledgment that even though their relationship had its limitations, they did not want those limitations to hinder this agenda was very important to him, and he responded. He himself was surprised that his parents initiated an effort to include them. This piqued Joe's

interest, and in his subsequent discussion with his wife he wondered if this was an unique opportunity in his family—one he might regret later if he did not take advantage of it.

Jane and Jeff responded immediately to the invitation in the sense that Jane said “yes” for them and Jeff didn’t say “no.” She ended up half-dragging him to the retreat, ignoring his objections that her parents have never liked him and never would. Jim and Jennifer were eager to attend, anticipating that changes were in the wind for Baker Pumps, changes that would strongly impact them, hopefully for the better.

## **Setting the Tone of the Retreat: Empathy and Rapport Revisited**

As the retreat begins, Fred Scott’s opening remarks set its tone and help shape everyone’s curiosities and uncertainties. With the agenda clearly spelled out on the board behind him, he stands to speak. “I’m Fred Scott, Bob and Sue’s attorney,” he begins. “I’ve counseled Bob for the past 15 years or so at crucial points in the growth of Baker Pumps. Bob and I have come to know one another quite well in that time, and we speak directly and honestly with one another. This retreat was my suggestion to Sue and Bob. Baker Pumps is at a critical point in its history. Probably no other time has been more important except the original start-up period. Any critical period in a business is a time of anxiety and uncertainty.”

“This is for two reasons,” Fred emphasizes, “the uncertainty of entering new territory and the fact that so much is at stake. First of all, the business owner and/or the business have never been on this part of the road before, and there are few road signs or maps. That’s where professionals like Bill Smith and I come in. We’ve worked with families with small businesses, helped them negotiate these transitions, and created the maps and signposts for the journey of succession Baker Pumps is now facing.”

“Bill and I have found that creating solutions to empower family members while meeting business needs is the key to the success of families with small businesses. Bill’s specialty is helping foster solutions that enhance family businesses. My specialty is helping the owners design succession and estate plans that will achieve their business and personal goals. Today my role will be to focus on the ‘content’ of the discussion. I’ll take notes on its high points, note conclusions reached, and make a follow-up list of action items. Bill’s role is to focus on the ‘process’ of the discussion, to keep the items listed behind me on the agenda, to orient it to positive options and solutions as we move along, and to solicit the active participation of all of you here today.”

“The second reason for the anxiety that accompanies a business succession,” Fred continues, “is the fact that so much is at stake for any small business. To an outsider, and even to family members, a developed business may seem like a supertanker—gigantic, stable, and able to navigate any economic weather. To a founder such as your father, however, the ship called ‘Baker Pumps’ always feels like a supertanker that needs constant vigilance to avoid becoming the next Exxon Valdez or the Titanic with some unseen vulnerability that can quickly sink her.

And all of the family members, employees, and customers who have depended on the good name and character of the Baker company would suddenly find themselves adrift in the economic marketplace.”

“In actuality,” Fred continues, “the truth lies somewhere in between. Baker Pumps is an established company with an excellent record in the community. Yet for it to survive, it cannot depend forever on the blood, sweat, and tears of ol’ Captain Bob. Bob and Sue have made it clear they want to plan for the next generation to manage Baker Pumps, and how to make that happen is what this retreat is all about.”

Bill Smith then stands to address the Baker gathering. “Few people,” Bill begins, “understand what it’s like to live in a family with a small business. Those on the outside believe that a small-business family is just like any other. Dad goes to work early and comes home later than he would like. For Bob and Sue’s generation, Mom supports Dad and is the primary caretaker of the children. And the kids grow up oblivious to what Dad really does all day at work.”

“But in a small-business family the story is quite different. Dad never leaves work because he brings it home with him. And not just in his briefcase, but in his worries, anxieties, and frustrations of the day. Dinner conversation more often than not is about the family business, and customers, employees, friends, and acquaintances in the community who flow in and out of the business day. The children in a family business, chances are, know many of these individuals personally and go to school with their children. A conflict involving their father’s business day becomes theirs when dad comes home to dinner and talks about it. If that conflict involves a family the children know, they carry that conflict with them to school. The children become part and parcel of the family’s network of relationships, even though when young they do not have a direct role in the business.”

“As the children grow, they may take part in the business, working with dad on weekends or evenings. Or they may work summers for dad. They get to know dad’s employees and customers. They see the community from a very different perspective than the kids whose families do not operate small businesses. And while their counterparts may be spending time at Little League, or cheerleading practice or Scouting, the children of a small business may instead be ‘helping out’ down at the shop.”

“And Mom’s role is different too. She is not just the mother of the children. She is also the mother of the business. Her role is usually that of a behind-the-scenes cheerleader. She will urge dad to talk about an unusually hard day. She too knows the customers and employees who inhabit the world called ‘Baker Pumps.’ She knows their spouses and their children. Her role and status in the community—in neighborhood, school, church, or synagogue—is shaped by the reputation and status of her husband’s business in the community. Often her friends will be determined by the relationships her husband develops in his business.”

“And what else about Dad? Chances are, as the creator and operator of a small business, Dad is a pretty isolated guy. This is not because he cannot make friends or because he is

unlikable. But few people have any idea of what an entrepreneur's life is like. He does not have a nine-to-five job. His responsibilities do not end when he goes home. At dinner in the loving faces of his family he faces potential disappointment and embarrassment if his business efforts should fail. He has taken enormous risks to follow a dream that no one publicly shares. This is not because his wife and family do not care about him but rather because all his efforts are, of necessity, focused on establishing and maintaining the business. At the end of a weary day he often doesn't have the time or energy to share his victories let alone his defeats with them."

"The small business owner is a jack-of-all-trades and a very smart guy. Yet he knows his own weaknesses all too well and hopes no one will find them and exploit them to their business advantage. He shoulders enormous responsibility and does so willingly. Yet his failure would directly affect many more people than a corporate executive whose firing affects primarily the livelihood of his own immediate family."

"So when a small-business founder succeeds, he or she has won out over great odds. In any given year thousands of small businesses fail. The small business is continually filled with challenges. For the business to pass to the next generation, it must have in place a management system that will successfully weather the transition. This task is perhaps the greatest challenge a small business faces. How do you transfer a dream? a vision? In reality only about one in three small businesses makes it to the second generation and only one in three makes it to the third."

"So Baker Pumps stands on the threshold of a generational transition, ready to either be sold or transferred to the next generation. Bob and Sue, you have much at stake. While you have been financially successful up to this point, your entire financial future is dependent on what you decide about Baker Pumps. The company is an asset you have built and nurtured for three decades. Unlike stocks and bonds or real estate, which have an easily determined fair-market value, Baker Pumps gets its value from three things—its continuing production of a revenue stream, the value of its equipment and real estate, and its potential for future earnings. In the wider marketplace to a potential buyer, the fair-market value of Baker Pumps would be quite subjective. The integrity of the founder and his reputation for success may have no tangible value to an outside purchaser. Yet from the inside these qualities have been key to the business's success to date. Ultimately both tangible and intangible factors will determine what value Baker Pumps will have for the Baker family."

Now Fred Scott stands to speak again. "Bob and Sue have talked with me about the business and also about their estate. They are wise to begin their estate planning at their ages. So many individuals do it much later, and many never do it. Because Bob and Sue are forward thinking, they have reported their assets to me and asked how they might best be utilized for their future. Some of these considerations involve legal and financial arrangements, which we will discuss later. However, the linchpin of their estate is Baker Pumps and what they decide to do with the business will determine how the rest of their estate plan falls in place."

Fred continues. "Experience shows that most successful businesses have an effective management team to operate the business, competent professional advisors to provide counsel on

business matters, and often an outside board of directors to provide guidance on business strategies and long-term planning. The immediate issue at hand for Baker Pumps is the question of management succession when Bob retires. I'll turn the discussion back to Bill for this portion of the session."

Bill stands again and begins. "In any organization, large or small, the transfer of power is a delicate issue. That's because who ends up in charge affects so many people. Their status in the organization, perhaps potential financial gain or loss, and even perhaps the satisfaction arising out of their daily relationships may be affected by the succession decision. Nowhere except in the small family business, however, does the succession decision have such an enormous personal consequence. That's because the fate of the entire business lies in the hands of its founder."

"Being an entrepreneur is a lot like being a one-man band. Actually in the beginning that's exactly what it's like. The founder does everything: planning, design, manufacturing, sales, billing, and clerical work, and then sweeping the floors, taking out the trash, and fixing the plumbing to boot. Eventually, individuals are hired to carry out these functions. They even have titles and formal responsibilities. But in a small business, it's always the founder who is the glue that keeps everything together. Just think, Heaven forbid, if tomorrow Bob is called to his Higher Reward and is not here to run the business. What would Baker Pumps be like? Likely not a pretty picture and one I'm sure everyone in this room has given thought to from time to time."

"Compare for a minute Lee Iacocca's departure from Chrysler Corp. Did the company miss a beat? I don't think so. Was Manufacturing affected? Sales? Billing? It's a very different picture. In a small business the founder has his hands in everything. That's because he himself created everything! And he probably knows how to do each person's job in the company better than they do themselves. Am I right, Bob?"

Bob smiles and nods. "That's for sure."

Bill walks over to Bob and puts a hand on his shoulder. "Well, Bob. In a nutshell that's the dilemma of every small-business owner. You still remember the business like it was yesterday. But chances are you no longer *want* to do everyone's job better than they can. That's because the positions in Baker Pumps have become very sophisticated and even more demanding since you began. This is a terrible burden because it can distract you from actively planning for the business without yourself at the helm. How can you maintain the quality assurance function without having that 'hands on' control of old? And if you're standing in the wings, who can possibly guarantee Baker quality in a business that's grown so quickly? Maybe the rest of you in the family really cannot understand Bob's dilemma here, because you haven't been in his shoes. So Bob would you say a few words about what it's like, wondering how Baker Pumps can succeed without Bob Baker at the helm?"

Bob looks a bit sheepish, but he feels Bill truly understands what it's like to be the founder of a small business and what it's like to be in his shoes. "Well, I guess it was once like climbing a mountain, getting to the top, and enjoying the view. But now I'm trying to figure how to get



down from the top in one piece. I figure I'll need some help, but I'm not sure who's the best to get me where I want to go."

"That's quite a picture, Bob," Bill observes. "Say some more about what it's like looking down from Mt. Everest."

"Well, it's exciting and scary," Bob replies. "I'm pretty proud of making Baker Pumps into a \$3 million business, and I'm grateful that Sue and I have been able to raise and educate the kids in a style most of my neighbors couldn't afford. But Fred knows that as much as I believe in planning and analyzing every aspect of a business decision, looking at the future of my business is something I really haven't thought much about. I see a lot of risk here, but not a lot of upside."

## **Inclusion and Group Participation**

"That's exactly why we're all here this weekend, Bob," Bill replies. "Thanks for giving us such a clear picture of the founder's dilemma. What do others of you think about what Bob just said?"

Sue responds first. "I know this decision has been bothering Bob a lot. And I'm concerned too. I may not be in Bob's shoes, but I've known the business from the beginning too. It's a big business. I don't know how Bob has done it all himself for so long. I worry about his health, and I want him around so we can have a retirement together. But I don't see how he can let go at this point. There's just so much that's involved."

Jane responds too. "Daddy, I see how hard you've worked over the years, and I see what's happening to your friends every day—heart attacks, cancer, strokes. No one wants to find themselves with a major illness. However you and Mom do it, I hope you just figure out a way to get the business off your back."

"It's not *that* bad, Janie," Bob complains.

"But it can be, Daddy," Jane persists. "Look at what happened to Sam Cohen—seemingly at the peak of health, a jogger, and yet a disabling heart attack at 62. And Sam's wife is struggling to keep their insurance business together at all costs. I just don't want that to happen to you. Look what happened to Grandpa."

"But I *like* running Baker Pumps," Bob retorts. "I don't want to work at the same hectic pace, but the company has been my life."

"And it can still be your life," Bill Smith interjects. "But perhaps its time to take on your next role in the business—that of a teacher or mentor, rather than the 'doer.' You really play a unique role, Bob. Only you know every facet of the business. Only you can completely teach someone all this information. Yet to take on this new role, you have to be willing to see yourself differently—more as a statesman."

“I’ve never been a statesman . . .,” Bob begins to protest.

But then Jim jumps into the conversation. “Dad, you are a statesman every day. Look at the way you handle difficult customers. They come in complaining to high heaven and walk out with a smile after you’ve spoken with them.”

“Yeah, but that’s no big deal . . .,” Bob begins.

“But,” Jim interrupts, “look at all the people who come to you for advice—the paint store owner, what’s his name—ahh, Steve Porter—who wanted your thoughts before doubling his size, and the banker who wanted your confidential assessment of some of his commercial loan prospects. And then every week at Rotary when I see people coming up to you for your ideas. You’re more of a statesman than you think.”

“Those are astute observations, Jim,” Bill observes. “You really know how to point the conversation in a positive direction. We’ll come back to that later. So you see your Dad with all the necessary skills, and others are already relating to your father as a statesman. What’s your reaction to that, Bob?”

“I never really thought of myself as a statesman. People do seek my advice, though. And the *Marine Pump Monthly* did interview me as Entrepreneur of the Year, so I guess that counts for something.”

“You probably have accumulated more wisdom over the years than you imagine,” replies Bill. “Most entrepreneurs do, but take it for granted. It really is a valuable commodity. And it can be an enormous resource as you contemplate the next phase of your business.”

“How’s that?” Bob wonders aloud.

“You understand the inner workings of your business as no one else does,” Bill continues. “You know what makes it tick—its strengths and weaknesses. You have the big picture, yet you know the thousand little details. Don’t you agree, Jim?”

“That’s for sure, Dad. I’m always surprised about what you know about the littlest of details. I don’t know how you come up with some of that stuff.”

“And that’s just what your Dad needs to teach his successor, the inner workings of his own judgments and assessments that are not apparent to the outside observer but which make for the continuing success of the business,” Bill concludes.

“And it sounds like you’ve been doing lot of learning from this great teacher yourself, Jim,” Bill notes. Jim smiles in agreement as does Bob.

Jane intervenes. “I really understand that, but I have always assumed Jimmy would be Dad’s successor. He’s the only one of us who has really been interested in the business, and he’s worked alongside Dad for years now.” “That’s one of the topics for discussion today, Bill replies. “To put it in a true management perspective, let’s pretend for a minute that Jim is not a member

of the family, but that he has been an employee of the firm for a number of years. Interest and tenure are nice qualities to have, as Jane assumes, but what other qualities are also needed to run Baker Pumps? Let's ask Bob what he would be looking for in a managing successor and assume Jim isn't even a candidate at this point. Bob, what management qualities will it take to keep Baker Pumps a success?"

## **Homing in on Business Succession**

"I've never really thought much about it," Bob says, a bit surprised. "I guess I would want a take charge kind of guy, someone who would care as much about the business as I do."

"Sort of like Jim did when he encouraged you to see your role as a statesman?" Bill asks.

"Why, as a matter of fact, yes," Bob says, his gaze shifting upward as he starts to sort through this information. Bringing himself back to the conversation, Bob confirms, "actually, I think that's the most important thing."

"What other qualities come next, then?" Bill asks Bob.

"A master of the technical details of pump manufacturing, for sure," Bob continues. "And I guess someone who can manage people, too. I've got some guys who try to throw their weight around and need to be reminded at times just who's the boss."

"So technical know-how and being a tough manager. That makes a lot of sense. Anything else?" Bill asks.

Bob, who's on a roll now, quickly replies. "Well, next comes knowing the competition, market trends, stuff like that. You can't survive if you don't know what's going on around you."

"That's an impressive list," Bill observes. "Let's see now. Let's write on the flip chart here the qualities of a successor for us all to remember." Bill writes the following.

### ***Qualities of a Successor Manager***

1. ***Takes*** charge
2. ***Cares***, has a sense of ownership
3. ***Good*** technical manager
4. ***Tough*** manager
5. ***Has*** market savvy

“Any other details you’d add?” Bill asks Bob.

“Well, there’s finance, computers, sales, and all that kind of stuff,” Bob muses. “But you can pretty well buy those skills anywhere. Or today there are professional firms who can advise you on these matters. Still it’s nice to be conversant in these areas.”

“OK, so let’s add one more general category,” Bill concludes. And he writes on the list:

## 6. *Understands* operations and sales

“Yeah, that’s pretty well it,” Bob says with a sense of satisfaction.

“Now whom have you ever met who can fill these shoes?” Bill asks Bob.

Suddenly, the oldest child and first son, Joe, who has listened with great interest to this point, chimes in from out of the blue. “Superman! that’s who. There’s no one person other than you, Dad, who could ever even attempt to fit that list.”

Joe continues. “That list is so unrealistic! It could apply to my architectural firm, too. But we have three partners to do all that, and we’re all stretched to the limit. I really feel for Jim or anyone who has to fill your expectations.”

Bob is taken aback by Joe’s outburst and isn’t sure what to say. Deep down inside he knows the truth of what his older son is saying. But he is embarrassed by the tone and intensity of Joe’s remarks. Joe has never spoken to him in such a way, but before he can speak, Bill intervenes.

“Joe, you say that with a lot of feeling. Before anyone else responds, say some more about what you are thinking and feeling.”

Joe forges ahead. “Dad has always been a Superman. And none of us has ever been able to measure up to him—at least in his eyes. He’s built this successful business all on his own and he deserves credit for that. But he’s always made it clear that it’s his business and that no one else could ever do what he’s done. I remember his motto still from the time we all were young, ‘If you want to do it right, you do it yourself’ I can’t imagine him ever letting anyone take over the company.”

“But that’s what we’re here to talk about this weekend,” interjects Sue, defending her husband. “Your father isn’t like he used to be. I’ve been married to Superman for over 40 years, and I know him better than anyone. But he’s getting tired of it all, believe you me.”

Bill responds to keep the discussion on track and to channel the strong feelings onto a solution-oriented path. “Joe, I’m impressed with your admiration for your Dad’s abilities. I agree with you: he did build a great business and deserves credit for it. Bob, as does every successful entrepreneur, has had to be Superman to make a go of the business, just as I’m sure, Joe, you had

in order to be successful in your business. Superman's personal qualities of charisma, intelligence, and even a kind of charm have helped him be extraordinarily successful. But Superman—a.k.a. Bob Baker—is running out of steam. The fact is that Baker Pumps is a very different organization from the one Bob started thirty years ago, and the skills it will take for Bob's successor are very different from those it took to launch the business then. It's no longer in a start-up phase; it's in a maintenance and new-growth stage, which takes a very different kind of boss. As Joe has pointed out, a formalized management structure may be more appropriate now for any large business than just the strength and charisma of a Superman, which once worked so well. To stay competitive now may take more than one person to do the multiple tasks of managing a growing business."

"So where does that leave me?" Bob asks rather angrily.

"Perhaps Superman wants to stop and smell the roses, spend more time with Lois Lane and the family," Bill begins. "But maybe he fears there is some Kryptonite in those roses too. Slowing down is not always as simple as it seems; but because of your dedication and hard work, you are in a position to write yourself a new job description—one equally important and more fitting to what you want out of life now," Bill answers. "Just as you have met every challenge for Baker Pumps in the past by learning something new or getting professional advice, or at times just winging it, you have yet another new challenge. This one is called 'succession.' In many ways it's no different from any previous challenge you've had, because you will use the same skills that have served you so well in the past: your natural business acumen, your intuitive sense of people, and your commitment to the success of your business."

"As with everything else in life, there's always the good and the bad, the advantages and disadvantages. You worked hard and created a successful business, poured yourself into it so it would grow and expand—and it did! Now it's big and it's beginning to feel like a heavy burden you have to carry all the time, leaving little time for anything else in life—and perhaps contributing stress that could diminish your health and your future. And you've told me you want more out of life—time with family, vacations here in the Keys. So because you were so very successful, the success of your business has also become a disadvantage."

Bill continues, "Turning the business over to someone else may be an advantage in that it would free you up from the daily burdens of the business. But the disadvantage would be letting go of some of the control. Only you know when the advantage will outweigh the disadvantage. But then again, maybe every disadvantage is also an advantage and the advantage in letting go could be writing a new job description that more perfectly fits your life now."

Bob sits in active but silent thought. He has conflicting emotions—frustration at the truth of Joe's remarks, which deep down he knows is on the mark, and relief with the caring way Bill Smith has framed his dilemma.

## Reflection on the Family Process

There's a pause in the conversation while Bob—and everyone else too—considers what has happened. Bob realizes the reality of his desire to let go, for indeed this is what has been keeping him up nights. The problem has never been laid out clearly yet gently in front of those whose opinions and respect he values the most, his family. This is truly a critical turning point for any entrepreneur. It's deeply troubling to realize the strengths that have propelled you this far in life seem suddenly to be liabilities. And for entrepreneurs, doing it all by themselves has an isolating effect on family members that can be tragic. Many entrepreneurs never share with their loved ones what it is that drives them: like Bob, they have dreams—unique dreams. At first they are perhaps vague notions, but with thought such ideas grow into a full-blown sense of personal mission. Yet entrepreneurs often have an unspoken belief that restrains their talk about themselves, perhaps to avoid burdening families with problems, or because fears of failure, worries, or anxieties get in the way. Better not to admit a vulnerability. But whatever reluctance there is to share difficulties with family—or even the dream itself—the entrepreneur goes it alone; and a cost of success is that those who love them ultimately do not understand them or help them let go.

Sue understood early on and accepted her role as the spouse of an entrepreneur. The strength of their relationship, built on love and mutual respect over the years, has made it possible for them to come to this point—a thoughtful and careful consideration of how to make their retirement the success that the business has been. However, Bob has never shared his vision with his children; he was just too busy. Growing up, they never understood why dad was absent from home so much. As they grew into adulthood, they had no sense of the vision that motivated him. Nor did he ever share his secret desire that someday his sons would succeed him in the business. Consequently, over the years there was much misunderstanding of their father and much miscommunication, the consequences of which are becoming apparent at today's family retreat.

So Bob's success has had a direct effect on his kids, but it is not the impact he envisioned. The alienation of Joe, their elder son, has puzzled both Bob and Sue. Most every son wants to grow up to be like his dad, and Joe did too. As soon as he became a teenager, Joe was always down at the shop. Since he was naturally mechanical like his dad, the employees, like Ed Jones, befriended him and taught the eager student about pumps. Dad was always too busy with the challenges of running the company, so Joe found others willing to teach him. That was the reason for his fury at the dinner table at the age of 12 when his father fired Ed. Joe stomped off and his alienation from his father and the company began to fester. As Joe grew into his teens, his mechanical aptitude continued to grow too, showing itself in first place awards at science competitions and displays at the State Fair. Bob was always so busy that he never noticed his son had the skills, talents, and interest to be a ready and willing candidate for the successor he would need some twenty years later.

Joe reports that it wasn't just being ignored by his father that led to his alienation. At every turn when he would want more involvement in the business, Dad would say he wasn't qualified. When Joe wanted to answer phones when he was 16, Dad told him he "didn't have the skills."

When he wanted to work for Dad upon graduating from high school, Dad said he “better go to college.” And when he considered mechanical engineering as a college major, Dad wondered if he really “has what it takes.” Feeling shunted aside time and again, Joe finally decided that he would take his own course with a vengeance. He changed his educational program to architecture, graduated with honors, and began to detach himself from the all-consuming culture of the Baker family business. Joe’s comments at the retreat have a double edge to them. They are observations of his father, yet they are also delivered with emotion filled with years of unresolved hurt and resentment.

Bob contends that his intention was never to push Joe aside. He was driven by his own idealistic standards of perfection and work, and in that game the son could never win. To Bob, Joe was never “ready” to meet the high requirements he believed were part of his own mission.

There was another factor, too. The relationship between father and sons by nature can be highly competitive. Bob’s own father had been highly controlling; and to do right by his own sons, Bob kept them on a tight leash. Bob’s intent was not to keep them down; it was the way he assumed parenting should be.

As they grow in independence, sons naturally bristle at this fatherly control: they want to show what they can do, and they want their fathers to be proud of them. Ideally, a father could see this as a natural motivation for success and achievement and would help his sons develop their talent, gauge their own skills in relation to their peers, and support them through the confusing teen years of sorting through values, personal competence, and ambition.

Many entrepreneurs, however, have their attention focused elsewhere. Bob perceived that Joe’s drive to succeed was directed *against* him, when in reality it was his attempt to *emulate* him. The grain of truth in Bob’s perception is that sons are competitive with their fathers; but this is a natural and primary way they gauge their abilities, level of talent, and sense of self-confidence. Bob was so focused on competing and proving how capable he was day in and day out that he had little time to do more than push them aside or be tyrannically “tough” in the only model of a good boss/father he had ever learned.

Bob is a bright and capable man, however—always ready to overcome challenges. Over the years he quietly realized that his relationship with his older son had soured, and he resolved that he would not make the same mistakes with the younger one. With Sue’s prodding, he responded to Jimmy’s early interests in the company. When Jimmy was a teen, Bob would take him aside and show him the “magical mechanics” of pumps. Bob had forgotten how much pleasure he used to get in working on a simple pump—not just repairing it, but thinking how it could be made better. His recovered enthusiasm for mechanics infected Jimmy by osmosis. It was something very special just the two of them shared.

In later years, Bob also began to realize how limited his relationship was with his daughter. He always assumed that she would never be interested in the world of his business. If the truth be known, Bob always treated Jane as a delicate princess; she was the girl her mother had always wanted, and both of them doted on her in ways they never did with the boys. It never occurred to

him that this tender and frilly female might have a place in the masculine world of mechanical pumps. As Jane bore his grandchildren, however, Bob began to see her in a new light. He was quietly amazed at how competent she was as a parent, how able she was to “take charge” of her family and its whirlwind of activities. And he couldn’t have been more surprised than when her youngest reached elementary school age and she went back to get her teaching degree—in an area that shocked him—teaching elementary school math and science! It is to Bob’s credit that he saw the limitations of how he once viewed his children and that he quietly resolved to improve these relationships when he could, notwithstanding that Jane’s marital difficulties saddened him.

Repairing relationships is not the same as repairing a pump. But Bob intuitively knew that at the retreat he would need to listen to his children. Listening was never his strong suit. He was always a step ahead of whomever he was talking to, had a better idea, or quibbled with some detail of a suggestion he was receiving. Over the years he had sought assistance from experts, such as C.P.A.s in areas with which he was not familiar. He knew when to ask questions and when to trust their judgment. So reflecting on the upcoming retreat, he realized he did not have all the answers, and he decided to take a chance and listen. “What the heck,” he told himself. “I can do whatever I want anyway.” This, of course, is the seductive dilemma of the successful entrepreneur. Bob has done whatever he wanted and has done it successfully. The problem is that he is now on totally new territory. Succession involves making judgments about others (something Bob has been pretty good about) and also about his *own* abilities, including his needs and problematic areas (something that is often more difficult). Forging ahead with a show of power and charisma has always worked in the past, but it will not solve the kind of problems Bob now faces. Does he have the kind of deep, inner strength to begin to let go of the control he has exercised over his business for years and begin to hand off the business to the next generation? “Letting go” of that kind of power means accepting change—change at the deepest levels of how he deals with the world—both in terms of his belief about who he is and in the daily satisfaction that comes from running a successful business created by the sweat of his brow and the work of his hands.

## **The Key to Business Succession**

Bill Smith picks up the discussion. “So what has to happen, Bob, for Superman to feel comfortable enough to lay down his cape?”

Bob replies, “First I’d need to know the business is in good hands. I can’t imagine retiring without having that confidence.”

“Right,” says Bill, “but that’s the final goal. Let’s think first about the steps to that goal.”

“Well, first I have to have a qualified successor. It may surprise, Joe, but I use to think someday he’d fill my shoes. I thought his architecture thing was just a fling and that someday he’d return to the family business. When he became so successful, I knew he’d never come



home, so I never said anything.”

Bob’s comment catches Joe completely by surprise. “I never knew you wanted me to be part of the business!” Joe says in shock. “I thought you definitely did *not* want me to be part of the business. You never encouraged me, and you said in many ways that I didn’t have it in me.” With pain in his voice he continues, “Dad, why didn’t you ever say anything to me?”

“I guess I was just too embarrassed,” Bob replies, “and too full of pride.” I realized that somehow I had pushed you away, but how could I admit that to my own son?” Bob’s voice is quaking just a bit. “It’s hard enough to say it now in front of everyone here. I didn’t know what to do, so I guess I just decided it was too late and let it go.”

“That’s a very powerful admission, Bob,” Bill observes. “It takes a lot of inner strength and flexibility to let yourself be vulnerable and admit the truth and even more in front of those you love. That’s true courage. With courage like that anything can be accomplished. This is a great start, Bob, and it’s maybe what Joe needed to hear. Joe, now that you know how your Dad really feels, how does that change your ideas about the company?”

“I’m still in shock,” Joe replies. “From early on I thought Dad didn’t want me around the business, so I just decided to forget wanting to be a part of it. That’s why I created my own. I’m glad to learn differently, but I’ve got my own company now. So even though I’ve always wanted to be part of Baker Pumps, I couldn’t be involved in the management side anymore. Maybe I could help out in some other way, though. I might like that a lot.”

Moving the impetus of the moment forward, Bill goes on. “Bob, how good to know your capable son would offer his good hands to the business. Is this what you meant by ‘caring, sense of ownership’?”

“I do want someone who cares about the business as much as I do, that’s for sure. I’ve always known how committed Jim is to the business, and now maybe Joe could be involved too. Having my sons run Baker Pumps would be a dream-come-true. But there are a lot of loose ends here,” Bob speculates.

“Let’s keep working with your succession list,” Bill responds, “and see where that takes us. Bill restates the list for all to recall.

### ***Qualities of Successor Manager***

1. ***Takes*** charge
2. ***Cares***, has a sense of ownership
3. ***Good*** technical manager
4. ***Tough*** manager

5. *Has* market savvy

6. *Understands* operations and sales

“Let’s turn to Jim. Jim, your dad just acknowledged that you too have a sense of caring about Baker Pumps. What do you think your strengths are as a manager?” Bill asks.

Eager to get into the conversation, Jim quickly replies. “I’m good with people, first of all. People at work like me and so do customers. I think that’s a great strength of mine.”

“Tell us some more, Jim,” Bill asks. “How is being good with people truly a management asset?” Bill asks.

“I do a lot of new business development, getting new accounts. Also when Dad’s gone, people come to me to make decisions. I try to get their ideas first before making a decision and have them have a sense of participation in the problem-solving process.”

“I never knew you did that,” says Bob quizzically. “Tell me more about that.”

“I know I don’t know lots of the details of the business,” Jim explains, “so I try to rely on everyone’s intelligence and experience. If I get stuck, I call Sam for advice if you’re not around, Dad. It’s not often, but he’s reliable and always gives me the straight scoop.”

“Is this the ‘take charge’ ability you’re looking for, Bob?” Bill asks.

“I was thinking more of someone telling others what to do, but I guess this is an OK way to take charge too,” Bob concedes. “I just want things to get done and in a good manner. Jim’s style would be OK if it works.”

“I noticed that Jim took charge of the conversation earlier,” Bill adds. “It sounds like Jim has ‘taking charge’ covered in both directions. Nothing like getting more than you asked for!”

“I’ve seen him work with groups of two or three engineers at times,” Jane offers. “Last week when I came to pick up the bank deposits, Jim was deep in discussion about that valve problem that keeps cropping up. Did you get that solved, Jim?” she asks.

“Actually, yes,” Jim answers. “But it was all of us together. We did get the job done, though!”

“This sounds like a different management style from yours, Bob,” Bill observes. “What do you think about this?”

“Hey, that valve problem was a big one. The proof’s in the pudding as far as I’m concerned. If it’s solved, I’m sold. Way to go, Jim,” Bob acknowledges.

“Thanks, Dad,” Jim smiles.

## Succession Details

“Are there strengths of Jim’s that others of you have observed as well?” Bill asks, looking around the room.

There are a few moments of silence, and then Jennifer, Jim’s wife, speaks to him. “Why don’t you tell everyone about your marketing ideas, honey? You’ve put a lot of thought into them. This seems like the right time to mention them.”

“I’ve been doing a lot of thinking about our market share, Dad,” Jim says turning to his father. “I know you have some strong feelings about developing new markets. But there are some opportunities I think are just too good to pass up in the Caribbean.”

“You’ve got that one right, Jim,” Bob flares. “Marketing is our Achilles heel. I’m not sure I’m going to like what I’m about to hear.” Jim pauses, debating whether or not to explore this issue with his father. Sooner or later they will have to work out this difference, so it might as well be here, Jim tells himself. As tempting as it is to avoid differences between his father and himself, Jim decides he will go forward. Not only is his wife sitting next to him urging him to proceed, but the family discussion so far today has been positive. So Jim decides to take a chance.

“I suggest we open our market into the Caribbean, though I know you have sloughed it off when I’ve mentioned it before. Do you have any idea of the potential for growth for marine pumps in that area, let alone in Central and South America? I’d like to know your reservations since you seemed to be so against this in the past. Are you concerned because you aren’t familiar with the culture and the market?”

Bob is surprised by Jim’s initiative. He responds. “You don’t know what you’re talking about. Foreign markets are filled with peril!”

“I know you’re not hot on foreign markets, Dad, but did you see the study the business school at the University of the Southeast did about the potential for those markets? There’s an article in the last issue of their quarterly business review written by one of my professors, Dr. Gutierrez. And I found it so intriguing that I had an hour-long telephone conversation with him. I also followed up to get the market research he recommended from the Data Research Institute in Miami. I haven’t taken the opportunity to speak to you about it, but there’s some important potential here for us!”

Bob is quite stunned at what his younger son has just said. Never before has he seen this side of Jim—one considering new initiatives, gathering outside resources, and presenting them to him in a compelling manner.

Before Bob can decide how to respond to Jim’s suggestion, Bill Smith speaks up. “Bob, to keep on track here, you don’t have to focus on the merits of Jim’s marketing suggestion today. We’re really talking about item #5 on your succession list, a manager who has ‘has marketing savvy.’”

“But you’re asking me to make a judgment about the marketing capability of someone who has an idea I think is just horrible,” Bob complains.

Jim replies right away and is not ready to back down from his point. “Dad, I love the heck out of you, and working for you is no piece of cake. But I don’t want just to be the boss’s son. I need you to have faith in me, whether we agree or disagree on things. I’m not sure if you’re against this idea because it’s coming from me or because it doesn’t have merit.”

“That’s a great question,” Bill Smith says. “How do you assess what Jim is saying? Do you have problems with the idea or with its originator?” Bill asks.

“I think I know what’s best for Baker Pumps,” Bob answers.

“That may well be true of the past,” Bill replies. “But we’re talking about the future of Baker Pumps and future markets.”

“And when the company was small like you said, you did know everything,” Jim adds. “But the business has grown enormously. Did you know that Jones Marine just bought acreage in Puerto Rico for a new manufacturing facility? Did you know they’ve filed a patent for a new valve that may revolutionize the business and take a hunk from our market?”

“I had no idea!” Bob says, taken aback. “Why, they’re a bunch of also-rans. They’ll never compete with us.”

“But, Dad, they are gaining on us,” Jim pleads. “We’ve lost two percent of our market share to them in the past year alone!”

“Why hasn’t anyone told me, then?” Bob challenges.

“We’ve tried to, Dad, both Sam McCall our plant supervisor and I have a number of times. But you’ve just waved us off with a flick of your hand. We’ve tried, really we have.”

At this point, Bob is beginning to see the outline of a new picture of Baker Pumps, a new picture of himself, and a very new notion of the capabilities of his younger son. “I guess I’m not on top of things as much as I thought,” Bob concludes with a depressing sigh.

Bill Smith responds. “Rather than see these developments as a defeat of your abilities, Bob, consider an alternative interpretation. You could see that Bakers Pumps is still in a highly competitive position and that through this retreat and your estate and succession planning you can position the company to compete at an even higher level.”

“I like that idea!” Bob smiles.

“And through its succession planning, Baker Pumps is facing challenges that have come as a result of its past success and growth. And it is to the credit of the founder and his spouse and family that they are assessing the degree of change required by their company to take it to new levels of success,” Bill suggests.

“That certainly sounds good,” says Bob. “And you know, I do want the company to succeed! The hard part is seeing it without me. As I see the resources I have within my family to keep the company succeeding, however, it’s hard to complain.”

“It sounds, Bob, as if you’ve made a major shift in your attitude about succession at Baker Pumps.”

“Yes, I guess I have,” Bob admits. By talking about Jim’s qualities as manager, I’m seeing a much bigger picture here. I just can’t see where I’m going to fit in.”

“Are you assuming it’s an all or nothing proposition, Bob?” Bill asks him.

Bob nods. “I guess I am, but so what?”

Fred, who had been listening intently to the interaction to this point speaks up to Bob. “Management succession isn’t a matter of pulling the plug on one CEO and plugging in another,” he observes. “It’s a transition, a process. The first question for today’s retreat was about personnel—who has the capabilities to eventually succeed you at Baker Pumps. But the next question is to decide how. This includes a list of steps, a time frame—typically three to five years—and a list of resources to be used in implementing the transition. Correct me if I’m wrong, Bob, but it seems that both you and Sue see Joe and Jim as resources for Baker Pumps in a way that you did not before. Am I right?”

Bob and Sue both nod simultaneously in agreement. “I think you’re right, Bill,” Bob concludes. “Maybe the idea of this retreat wasn’t so bad after all.”

After a moment’s pause, Jane speaks up. “Dad, I’m really happy you feel so good about Jim’s and Joe’s roles in your business plan. I don’t want to be left out as you make your plans. And I think Mom should have an active say in what will be happening too,” Jane says firmly.

Bob is taken aback by the words of his daughter. “I’m not clear what you mean,” Bob replies. “I mean I would like a direct role, not just that of cheerleader or supporter on the sidelines, Dad,” Jane responds. “Jim has been involved in the business for a long time and rightfully deserves a shot to run it alone. But I’ve been involved too, as my family demands have allowed. And I don’t just mean running to the bank with daily deposits. Who was it who found that Fran, your bookkeeper, was embezzling payroll tax payments and creating bogus receipts? Didn’t I say something to you long before the IRS came knocking on your door?”

“As a matter of fact, yes, you did,” Bob recalls. “And how are your receivables doing these days? Are they back in the high 90-day range?”

“Well, now that you mention it, they are,” Bob grimaces.

“Remember when your office manager was hospitalized and you had me fill in that summer when I wasn’t teaching? And how by autumn we had the receivables back down to the low ‘80s?” Jane challenges.

“I had forgotten about that,” Bob admits sheepishly. Rebounding, he asks, “what are you saying here? I’m not clear.”

“I’m saying that at points I’ve been very helpful to Baker Pumps, perhaps not in the spotlight areas like management or sales and marketing, but in the important area of office management and finance. And while I have the responsibilities of a young family and a teaching job right at the moment, perhaps I can still play some significant role in Baker Pumps. I bet, though, that you never really considered how I might be of help. Am I right?” Jane challenges.

Bob flushes, knowing that Jane is right. He had originally thought that the next generation of Bakers would someday be part of the family business but had never concentrated on what Jane’s role might be, thinking more of his sons’ participation. “I don’t know what to say, Jane,” Bob replies. “I’m embarrassed to say you’re right.”

Pressing on, Jane adds, “and I hope you understand just how significant Mom’s role has been to your success. She’s really taken the job of raising the family to free you up to focus on the business. I know that’s how you two worked it out, but did you ever think how your concentration on the business might have been diminished if you had had to change diapers every two hours?”

With that thought in the air, Sue intervenes, defending her husband. “Now Jane,” Sue admonishes, “you know that’s silly. I was always happy to raise you children. I don’t have any regrets.”

“I know that, Mom,” Jane responds, “but I’m making a point about how directly important you have been to Dad’s success. And I feel a lack of recognition by not being considered for any role in keeping Baker Pumps booming in the future.”

“I don’t think your father means to leave you out, Dear,” Sue responds.

“No, I don’t either, Mom. I’m not criticizing Dad. But as a businessman, how would he feel if he had made a major decision without taking every important resource into account. Wouldn’t he regret it later?”

“I would, indeed,” says Bob, having listened carefully to the conversation between his wife and daughter. “And you don’t need to defend me, Sue. I’ve lived long enough to know when I’ve overlooked something important. You’re absolutely right, Jane. I *have* taken your mother for granted. My mother always ran the household and wanted to stay out of my father’s hair when it came to the grocery business. I guess I just assumed that’s how it should always be.”

“I understand, Dad,” Jane says with caring, “but it’s that word ‘assume’ that’s the zinger here. If Mom has been happy with her role, that’s great. But I know that my generation is different. I like being involved in business. I like having the feeling of making some difference in Baker Pumps. I’m a Baker too, you know. And I’m not saying I want to have an equal role to Jim, but I would like to be involved in some fashion—maybe like Joe is going to participate. I don’t know. I have good math skills, and I think I know how to manage people pretty well, too.”

The group sits in silence for a few moments as everyone takes in the wisdom of Jane's words. Attentive to the process of feelings in the room, Bill Smith waits as the effect of her words sinks in. Then he rises and points back to the chart on the easel to item # 6, Understanding Operations and Sales. "It sounds to me that Jane has strengths in the area of operations that might be very helpful to Baker Pumps, Bob. What do you think?"

"I guess so," Bob says, taking a deep breath. "I've always known managing the office is important, but for me it's never been where the action is. I keep an eye on it, of course, but have to remind myself from time to time not to take it for granted." Then before anyone can speak, he adds, "Now don't get on my case, Jane," Bob grins. "I'm smart enough to see the parallel between taking the office for granted and you and your mother for granted. I'm not that dense."

Jane smiles back. "I never thought of you as dense, Dad, but it's nice to see you sensitive to this issue, especially since it's kind of foreign to your generation."

"Talk like that makes me feel old, Jane," Bob quips.

Jane isn't quite sure how to respond, but Bill Smith steps in. "Perhaps it's Jane's way of saying how proud she is of you to be flexible in a time of change, rather than wanting to chide you for being slow to change. Is that a fair statement, Jane?"

"It sure is. I've wanted to say something like this for a long time, but I haven't known how to tell you, Dad. This retreat is really helpful. I do want to be a part of Baker Pumps as best I can. That's really what I'm saying."

"I'm glad you spoke up, Jane," Bob replies. Then avoiding any reference to her marriage difficulties, he continues, "I did assume you had your hands full with family and career. I'd be delighted to have you involved with Baker Pumps. Office management is not one of my strong suits, nor is it Jim's either, I think"

Jim jumps in at this point. "Dad, you probably don't know how much Jane and I talk about the business, probably several times each week. I think it would be great to have her involved. Jane, I don't know how a full-time teacher could take on the office management of a \$3 million company and raise a young family, but I think we should talk about this some more, Dad," Jim says with great energy.

"It sounds good to me," Bob replies. "Jane, I welcome your involvement. I think we can work something out. As far as I'm concerned, you can be involved as much as you want to, but that's a decision you'll have to make. What do you think?" he asks, looking at her.

"I really want to give it some thought, Dad. I want to be involved, yet I do love teaching. But maybe working for Baker Pumps is a new opportunity. Is your retirement plan as good as my school district's?" she teases. Bob is caught short by his daughter's teasing. "Just kidding, Dad," she responds as she sees the uncertain look on his face. She gets out of her chair and comes over and gives him a big hug.

Returning to her chair, she finishes, “I do want to give this some thought and talk it over with Jeff. Then maybe you and Jim and I can talk further.”

As the discussion winds down, Bill Smith adds a reflection. “I want to say how impressed I am with you all today. You have had a wide-ranging discussion about issues that have been both challenging as well as sensitive. You have taken them on directly, and you have spoken directly with one another. The mechanisms you have in your family for problem solving, exploring ideas and solutions, and treating one another respectfully while you search for answers is a wonderful family asset. And it shows what can happen when you put your agendas on the table and ask others for their participation. Congratulations to you all.”

There are still points needing discussion to complete the business succession plan for Baker Pumps. But the Bakers are in a much better position to resolve them now that the family has been honest in discussing the habits that have limited them in their thinking about the future—Bob’s commanding style and its impact on his family and business and the family going along with his style and not knowing how to speak up about issues they feel strongly about. Based on the evaluation of Jim’s strengths and readiness to succeed his father and of Jane’s capabilities and desire to be involved, the stage is now set to discover how Dad, Jim, Jane, and perhaps Joe can more easily handle the transition.

The family ties within the Bakers have made such a breakthrough possible. While experiencing the conflicts and frustration that are part of life as a family grows, the Bakers have shown a reservoir of caring for and commitment to one another, allowing them to move through this emotional log jam. Not every family has these emotional resources or the reservoir of love developed over the years to carry them through the critical relationships involved in succession planning. Yet every family has resources to solve its problems and for better or worse has capabilities that can be accessed to find satisfying and lasting solutions.

## **Psychological Commentary**

In looking back on the participants’ interest in coming to new solutions, first of all, Bob and Sue have a strong investment in their future with one another and in their family. Their bond with one another is strong, and they deeply care for one another and their offspring. The challenges they find themselves amidst concerning the future of Baker Pumps are just that—no more and no less. Though they do not have the answers they seek immediately at hand, they turn to one another for those answers. In facing the challenge of their family business with so much at stake, they are willing to face the most difficult obstacle of all—major changes in the relationships with those they love and count on. They face the first obstacle in placing the calls to their children to set up the retreat. They continue their positive momentum in the retreat itself by listening to their children’s words and by responding to them with an eye open to the future. As they face these changes head on, they benefit enormously.

Sue has always been Bob’s supporter. In conflicts between her husband and sons, she has



never taken sides and does not do so at the retreat. She knows only too well the tough side of her husband, having lived with him longer than anyone else in the Baker family. Yet she knows too the vulnerable and sensitive man underneath the tough veneer. She does not judge him for his limitations, and she prefers to encourage his strengths. This has been her strength for over forty years. At the retreat she will quietly observe her children's challenges to their father and take pride in their maturity. She is surprised by Jane's direct interaction with her father and in speaking up for what she wants. In the back of her mind, Sue begins to reconsider her critical assessment of how well Jane has been handling her marital difficulties.

Joe and his wife are in an awkward position to begin with. Yet by coming to the retreat they send the message that they want to be included in the family plans. Joe takes a major chance by speaking his peace to his father. His father returns the compliment with candor and feeling. Their relationship shifts substantially as a result. No one could have predicted the result, yet the new tone of their relationship will no doubt have benefits for Baker Pumps and for the two of them as well. In addition, with the change in Bob's attitude toward Joe, other family members will feel freer to enjoy their own relationships with him and will feel freer to finally welcome Jill into the family.

Jim and his wife originally saw the family retreat as an opportunity to come to terms with the relationship with Bob and Baker Pumps. Having a ten-year working relationship with his father had raised lots of questions for Jim concerning his own business future. Would he ever get his father's assent to be the head man? Should he look to another company for advancement? He and Jennifer were up nights the week before the retreat deciding what questions they needed to get answered. Jim has a sharp eye on the market as his comments indicate. He sees his competitor's market-share gain and knows market opportunities in nearby third-world countries. His fear is that Baker Pumps is losing its preeminence and that his own future is in jeopardy as well. So Jim has a lot to gain by working diligently to resolve any problems with his Dad, convince him of his abilities and readiness, and keep the business in the family.

Jane, presumed to be the family cheerleader, experienced a different kind of ambivalence in her relationship with her father than her brothers did. A role for her in the business was never a real consideration by her father. As a typical middle child and as a woman, she seemed destined to have lesser status in the male-dominated Baker family. Her solution was always to help the home run smoothly. This is a strength she still brings to the family today, and she has brought this strength to the office operations at Baker Pumps. As a child she kept to herself her feelings about her father's ready involvement of her brothers in the business while she was ignored. As an adult, she has been supportive, but no longer at the cost of ignoring her own wants. The risk she takes in speaking directly and respectfully to her father is rewarded by his realization that he had underestimated and really ignored her potential to contribute to the family business. Unlike the teen who closed herself in her bedroom with rock music when family discussions got heated, as an adult she has developed a communication style that faces issues head on. This is clear in her risking a challenge to her father and in raising gender-related issues within the family.

The family adjourns for a break to relax and get some refreshments. There are still many

points needing discussion. But the Bakers are in a much better position to resolve them now that the family has been discussing the hopes for the future. Based on the evaluation of Jim's strengths and readiness to succeed his father, the revelation that Bob wants to have Joe involved in the business, and Jane's desire to be a participant as well, the stage is now set to see how the business succession can be accomplished.

## Reflections

1. Just as every family is different, every family retreat and every family conference will be different. In this session, one can see how the ways the parents and children have related in their family over the years do not necessarily predominate today. The challenge of business succession brings a new dimension to their lives, and the opportunity to create new ways of relating. This is the excitement of working with the family/business succession process.

2. The reader will recognize that the professional leaders respect all members' views and are able to build a consensus based on differences. They establish rapport with the parents initially and then with all other attendees at the retreat. They are able to do so because they believe the solutions for the Bakers' succession goal will come not from themselves—the so-called experts—but from the family members themselves. This professional distance enables Bill and Fred to support family members as they seek solutions.

3. Fred and Bill also share a philosophy that families have a history of problem solving as does each individual family member. For addressing the issues in management succession, this shared history is a great resource on which the Bakers can rely. As Joe, Jim, and Jane become more involved in the retreat discussion, they bring with them their strengths and resources to focus on the important needs of Baker Pumps.

4. Patterns of authority—how it is wielded and communicated—and parental tension between attention to business versus attention to growing children characterize all family businesses. The authors have chosen a traditional family structure for illustration, but it is by no means the only or even statistically prevalent family-business constellation today.<sup>5</sup> The communications specialist and the attorney are adept at navigating the Baker family into an exploration and discovery of strengths and talents because the two professionals have worked together in similar situations many times before. They understand that focusing on clear goals can keep family discussion on course and make it profitable, thereby keeping family members' involvement and sense of ownership in the process at a high level.

6. The success of a family retreat or conference depends on the motivation of the entrepreneur and his or her spouse. In many situations, it is difficult if not impossible just to get all the family members in one room for a discussion. The question of what motivates family business owners to begin financial or estate planning is a perennial one. Often an appointment with a professional advisor is precipitated by some event which is emotion-packed.

It might be a brush with death, as in a near automobile accident, or the death of a parent,

other loved one, or close business associate. This was the case with Bob Baker concerning his father's open-heart surgery, and his golfing partner's critical illness. Entrepreneurs who report incidents like these are excellent candidates for planning since their motivation is strong.

Why some individuals become sensitized to these concerns where others are hardened to them is never apparent. Individuals who claim seriously that "I'm going to take it with me" are seriously deluded and make poor candidates for planning. Their attitude toward their own mortality is one of denial, and to be taken seriously, no matter how absurd it may appear. Denial is an extremely powerful defense mechanism which appears very logical and sensible to the one in denial. Its absurdity is frequently apparent in cases of alcoholism and chemical dependency, and that is why substance abuse treatment focuses to such a great extent on patient's holding onto their denial. It is the vehicle for them to actively maintain their illness.

The substance abuse model is very helpful here because those in denial truly believe they are in control when in actuality they are out of control. Such a terrifying truly is comfortingly avoided through the mechanism of denial.

Theoretically, other emotion packed incidents such as the birth of a grandchild, the graduation of a child from college, or even older age couple adoptions can trigger the impulse to plan. These occasions of joy merit, even demand, good planning for the future. More often that not for the typical business owner, however, the daily demands of running a business over time become a distraction from the goal of planning. The question is always what brings the business owner back to the core of preserving and enhancing his or her business over the long run.

7. Other barriers to planning include procrastination. Almost as difficult as denial to deal with, the procrastinator's promises must not be taken at face value, only the repeated continuous failure to make a decision. Procrastinators, at least, are aware of their failure to make a decision, though not of the reason.

Procrastination, like denial, is motivated by feelings, not reasons. Procrastinators get enormous benefits from not making decision, and until those benefits come to light, the procrastinator will not change. The advisor can best simply ask what (horrible) consequence will occur if the procrastinator makes a decision. Ironically, it is often fear of some catastrophe. In more than one case, a client avoiding making the final decision on his estate plan has believed deep down inside that if he completed the plans around his estate, he would die. The grain of truth in this perception is that the client may believe he or she has nothing more to live for once an ultimate estate plan is completed. This is where the advisor can inquire about what the client would like to do for the rest of his life, or alternatively, suggest seeing a professional counselor who deals with such issues.

8. Frustrated professionals trying to "motivate" a "difficult client," may lapse into explaining the difficulty in getting planning going by labeling the client as controlling. This gesture by itself will only confirm the stalemate in the relationship. The professional can look deeper into the "control" issue, however, by asking how he or she would feel in the client's shoes. What would he or she do if they had as much at stake as the client does? And what

benefits does the client get from not making a decision.

“Control” also has many faces. Is the psychological currency of the “controlling” entrepreneur an ego issue in which he or she has to have all the answers to feel good about a solution? Or is it control born of mistrust in which the entrepreneur must handle or inspect every detail personally, in which case the role of the professional is essentially useless. Or does the control stem from a hard headed business model in which the entrepreneur knows the value of detail in determining success? In each of these cases, “control” exhibits itself differently, and calls for a different creative response from the professional advisor.

9. There are several different methods of structuring businesses to facilitate the smooth transfer of control to succeeding generations. In the case of the Baker family, Jim seems like the obvious successor in terms of the future control of the business, although, he needs significant mentoring to develop the qualities of a successful manager. Neither Jane nor Joe desire to become successor managers or majority owners of the business and, therefore, Bob’s choice of a successor is clear. However, in many family businesses the owner faces an extremely difficult choice in how to structure the business to facilitate transfer of control.

10. For many business owners the choice of business organization involves deciding between giving control of the business to one child who will then be a majority shareholder with the other children being minority owners. The advantage of this form of business succession is that one child who may have demonstrated exceptional leadership qualities will have the necessary control to make the tough business decisions that are necessary and will not have to constantly struggle to make decisions. This is not to say that his or her siblings will simply remain silent as to the operation of the business, but at least in terms of legal control the selected child will have it. The potential difficulty with this form of ownership is that the succeeding majority owner will often find bitterness and jealousy on the part of his or her siblings and as minority shareholders they will often create as much legal difficulties for him or her as they possibly can. The authors of this book believe the solution based methodology of dealing with business succession provides Bob and Sue (and perhaps all of the other family members) the opportunity to deal with these issues. This includes expressing their personal feelings and opinions, and allowing Bob and Sue to solve the problem of a successor owner in a way which takes into account the considered feelings and beliefs of all who will be affected by the decision.

11. Another possible form of business structure dealing with succession planning is to leave ownership and control of the business equally to all children. The advantage of this form of business succession is that all children are treated equally and none of them will feel slighted. The obvious difficulty with this form of business succession plan is that too many cooks may spoil the pot and the business will suffer because of an inability of all the children to agree on important business decisions. Frequently, under this form of business succession, all of the siblings will agree among themselves as to which child should assume the leadership role and submit to his or her decisions. Alternatively, to avoid future conflict, the children will agree to divide the business into separate divisions with each child managing his or her own separate division.<sup>12</sup> As mentioned previously very few businesses ever make it to the third generation

and in that regard typically at the third generation the ownership now is vested in various owners. This form of ownership obviously suffers from having numerous owners with often competing and conflicting goals for the business. This presents an extremely difficult challenge for succession planners. They must establish strategies to deal with the diversity of ideas and ownership. The authors believe it is highly advantageous for the business to employ family business consultants who are knowledgeable in creating an atmosphere of good communication among all owners and can obtain input from all parties involved to recommend and establish decision making structures.

13. In addition to helping to identify the proper form of business succession plan it is important that the planner deals with the potential problem of in-laws. Not only do family businesses face potential conflicts from competing children, they also face potential in-law problems concerning what happens to a child's ownership interest in the event of a divorce or untimely death. In either of these two situations ownership may fall into the hands of non-family members. In that regard two of the most frequently used methods of dealing with this problem are Shareholder Agreements restricting ownership of corporate stock to family members and prenuptial and postnuptial agreements wherein spouses waive their rights in the event of death or divorce. In the case of Jane, she is in a conflicted marriage. What might happen to her stock in the business if she were to receive stock and subsequently get divorced? One method of dealing with this problem is to place stock in restricted trusts with spendthrift provisions to prevent the stock from ever passing to non-family members yet providing to the beneficiary the right to receive dividends from the corporation.

## Chapter 4

### THE BUSINESS SUCCESSION AGENDA:

#### New Awareness, New Solutions

The family and the advisors have taken a break after the morning session. Lunch is brought in and everyone relaxes and enjoys it along with a view of the ocean from the Bakers' Florida Keys veranda. Bob has time to absorb the helpful information about his family, and he and his children now have the chance to begin relating to one another in a new fashion.

Sue and Bob have some time together as well. Neither had expected their children would be as involved in the discussion of the family business as they have been. And they share their pride with one another in the adults their children have become.

In addition, the chance to be together as a family is a special benefit for Bob and Sue. The Keys home has often been a retreat from the hustle and bustle of the world of Baker Pumps, and this weekend is turning out to be a very special time for the Baker family.

Bill and Fred chat with family members from time to time during the lunch break, but while everyone treats them cordially, these two know that this weekend is truly a Baker family experience. As facilitators, their job is not to become part of the family but rather to help the family weave the strengths and contributions of all members into the fabric of a successful succession plan. In the retreat experience, Bill and Fred are respected guests, but guests nonetheless. After lunch, Fred calls the family back together.

#### **Moving into Decision-Making**

"I admire you all for bringing forth such useful information this morning," Fred begins. "The founder's role in the family business and the issue of management succession is the core of any successful business transition. These decisions must be addressed as the foundation of a business-succession plan and for an estate plan for Bob and Sue. Let's return to the issue of management first with Bob's list on the flip chart. With this morning's discussion and wide participation in mind, let's rename it 'The Baker Successful Successor List.'"

#### ***THE BAKER SUCCESSFUL SUCCESSOR LIST***

1. *Takes* charge

2. *Cares*, has a sense of ownership
3. *Good* technical manager
4. *Tough* manager
5. *Has* market savvy
6. *Understands* operations and sales

“After this morning’s session, Bob,” Fred asks, “what are your thoughts now about a successor for your business?”

“I see Jim in a new light, that’s for sure. He’s been involved in aspects of the business of which I had no idea. And I guess I’ve been afraid to loosen the reins on him to see what he really can do. (Jim and his brother and sister smile in agreement). But my problem remains. I have a multi-million-dollar-a-year business, and handing it over is still a pretty frightening thought.”

“Bob, you’ve hit the nail on the head. If you were to hand it over today—all at once—that could be frightening. What you need is a careful, step-by-step transitional plan that keeps the business in your hands while also giving Jim more and more of the reins until you’re satisfied and comfortable and he’s satisfied and comfortable.”

“You mean it’s not an all or nothing deal,” Bob notes.

“Exactly,” Fred responds. “Business succession is a gradual process, perhaps taking a number of years with certain built-in benchmarks along the way to review progress before the next step is taken. Moreover, it involves a number of players in addition to the founder and his successor. Today, our discussion has involved the immediate Baker family, not just Jim and you. Baker Pumps has succeeded because of the many relationships you have built up over the years, Bob. Now you can begin to use these relationships as a resource in making the critical transition for Baker Pumps.”

“I like the thought of that,” Bob responds.

“And I’m sure you didn’t create those relationships with the thought of helping you hand off your business and secure your retirement. You created them to help you make Baker Pumps the success it is; and because they have been so effective, they can be a wonderful resource for you at this critical juncture,” Fred explains.

## **The Role of Employees in Succession**

“There is another side to the network of relationships that supports Baker Pumps,” Fred continues. “There are people, especially employees, who will not be supportive of the transition, who actually may be inclined to undermine it and whom you, Bob, are going to have to bring

along to actively support the new arrangement. This is not the easiest thing to do; but you've mentioned you don't want to put Jim into a failure mode, and carefully assessing key employees is a must if he is to succeed."

"Why, I can't imagine who wouldn't want Jim to do well," Bob wonders out loud.

"Boy, I can," Jim responds taking charge of the discussion. "Tom Phillips comes to mind right away."

"Tom—Tom Phillips?" Bob says in shock. "You've got to be kidding. Tom's been with me almost from the beginning. He's been my most reliable employee."

"Actually, Dad, he's been your most brown-nosing and free-loading employee," Jim retorts. "When you're out of the office, he literally stops working. He should own shares in 'Dunkin' Donuts he's down there so much on extended breaks. Sometimes we have to call him there and have him come back just to keep some projects on time."

"And I see his car there often when I'm running errands for you, Dad," Jane adds.

"You've got to be kidding," Bob says. "Tom's incredibly loyal to me. Always has been."

"When you're in the shop, yes," says Jim. "But his loyalty is skin deep. Remember that trip we took to Orlando for the training conference on pump technology? Well, Tom never went to any of the sessions. Said whatever he hadn't learned in the last 30 years couldn't possibly be important. He sat by the pool, and Sam McCall and I went to the training. At night Sam and I would go to dinner and compare notes on what we'd learned that day. Tom was nowhere to be found."

"I can't believe my ears," says Bob. Defending Tom he exclaims, "Surely there must have been a good reason. Why didn't someone say something to me? Why didn't you, Jim?"

"It's such a touchy issue, Dad," Jim replies. "We all know how close Tom is to you, and we just didn't know how to say it. We thought you'd just shrug it off, so we did nothing."

Bill Smith intervenes, "It is a difficult issue, to be sure. I am wondering what might be going on with Tom. For instance, he could be jealous of Jim, believing he, Tom, should really be in position to succeed Bob. Or he might be feeling left behind by the changes going on at Baker Pumps, technological changes for which he isn't prepared, for instance. There could be a number of reasons for his behavior."

Fred Scott comes back to respond to Bob's shock. "Actually Bob you'd be surprised how many times employees who began with the founder can take enormous advantage of them. That's because when the company was started, the employee was chosen more for an existing relationship with the founder than for particular skills. As the business grows and becomes more complex and demanding, some of these original 'friendly hires' just can't keep up. They spend their time—rather than changing to face new challenges and working to update their skills—covering up for themselves and trying to maintain the status quo. The result is a terrible loss to



the organization and its potential. For what reason did you hire Tom thirty years ago, Bob?”

“Well, . . . I guess just because he was there. We had gone to high school together and he seemed to know machines. He and I and Baker Pumps just grew up together,” Bob reflects.

“I think you and Baker Pumps grew up together and Tom came along for the ride,” Jim quips.

Fred adds to Jim’s remark. “That’s a pretty tough critique, Jim, but it’s probably right on the mark. No question, this could be a major problem. The typical problem in a transition is that someone like Tom finds his position threatened and will do anything to keep it, including sabotaging the founder’s designated successor even if it’s his son. Removing the dead wood from your company or retraining employees who really want to be part of the new team is part of the transition that you have direct control over, Bob. And though it is never enjoyable, it is a major succession requirement.”

Bob sits back in his chair. “I would never have thought that Tom was a laggard. I guess you’re on top of a lot more of the business than I ever gave you credit for, Jim,” Bob says genuinely.

“Jim, you seem to have some business savvy along with being so likeable,” Fred adds.

Bob continues, “But just to be fair, I’d want to give Tom a chance to be involved, but my terms would be pretty strict. And, Jim, I never knew Sam McCall was such a help to you. He always seemed so quiet I just assumed he had excellent skills but only an average commitment to the company. I’m glad you brought this to my attention.”

Bill Smith intervenes at this point. “And don’t think that you’re a bad judge of character, Bob. No one judges people perfectly all the time. It does tell you that others in your family can be helpful to you in this area. You may not only have *overestimated* the capabilities of some employees, on the other side of the coin you may have *underestimated* others. Your family’s assessments may be a succession resource you didn’t know you could count on.”

“Yeah, Dad,” Jim says with emotion. “Sam McCall has been a tremendous help to me. He’s really taught me the ropes and treats me like a colleague.”

“For what it’s worth, I think he might be one of the greatest assets you have in the business, Dad,” Joe intervenes. “He’s a great engineer. And as quiet as he is, nobody can push him around. I remember when I used to work in the shop, he wouldn’t let anyone get away with anything, not even me. And the men truly respected him.”

“Sounds like you have a key employee who can have a role in your business transition, Bob,” Fred observes, “and some sound judgment to count on from Jim and Joe.”

“I’m not sure I know what you mean,” Bob wonders aloud.

“Employees like Sam,” Fred continues, “know the business inside and out. If Sam is a

contemporary of yours and is a valued employee, you might want to develop a special employment contract for him, for instance for the next five years. Give him a promotion and a new title and status. Let everyone know. Then use his skills to mentor Jim.” Pointing to #4 “Tough Manager” on Bob’s Successor List, Fred continues. “If you think that Jim could benefit from even more toughness or savvy than he already has, give him an opportunity to learn from an expert. Make that a priority for Sam to teach Jim. The expertise Sam has developed over the years is invaluable. This kind of people savvy comes from experience. Jim has been developing it well, and imagine what he could do under Sam’s tutelage. And Sam has this savvy in your business. What do you think his reaction would be to this, Bob?”

“I think it’s a great idea! Sam does know his stuff, that’s for sure. I don’t know how he’d take to it though. I guess OK.”

“I think he’d really like it, Dad,” Jim responds, building enthusiasm. He’s been truly loyal in the business and I think a bit under-recognized. He and I really work well together. And if he knows his position will be safe during the transition, I think he would give his all for Baker Pumps.”

“I like the idea,” Bob reflects. “This is new to me, though. How do we make it happen?”

“You, Jim, and I can talk about this next week, Bob,” Fred answers.

“I might be able to help, too,” Joe responds. “I’ve known Sam a long time, and I can share some ideas about the mentoring we do in our firm, too.”

Building on Joe’s comment, Fred continues, “Bob, what do you think about you and Jim sitting down with Joe on the conference line, defining what Sam’s new role should be. Based on that, I can draft a contract for you to review. It doesn’t have to be complicated, but it does have to be clear. This is a great example of how a transition can involve others to ensure its success.”

“You might eventually want to ask Sam’s opinion about weeding out other dead wood, Honey,” Sue suggests. “You’ve mentioned concerns over the years about other employees, especially in accounting. Maybe Jane can help you in this way too. She knows all the employees, and she’s very perceptive about people’s talents and attitudes.”

## **Other Resources for Succession**

“Speaking of accounting, Dad,” Joe offers, “if you’re still on that old billing system, there’s some great software out now that can be standardized for any kind of business. We adapted some for our business and the receivables dropped in no time. The employees love it; and believe it or not, the customers actually understand their bills. It’s general ledger, billing, and a complete package.”

Before Bob can answer, Jane jumps in. “And a good billing system is just what you need to avoid problems like employees getting away with embezzlement! Joe’s idea sounds great to me,

Dad. I could help in implementing the system and training the staff. If it's like Joe's system, a general ledger system, I can help with that."

"It seems you have family experts in all areas of the business, Bob," Fred observes.

"I'm getting ideas from everywhere," Bob comments.

"I bet there's even more everyone here can learn from each other," Bill adds. "Look what we've already discovered in just a short time."

"That's what so nice when you share your vision for the future, Bob," continues Bill. "By letting others know what kind of future you envision, others are free to contribute, to support you, and to feel a valuable part of the process. That's quite a gift to them, and they return the gift to you by sharing their ideas with you. It's a pretty terrific synergy."

"That's how I feel about my relationship with the business school at Southeast," says Jim. "I keep in touch with my professors and call them from time to time. They always want to take the pulse of the everyday business world for their lectures; in turn they keep me informed about current market trends, economic cycles, and even legislation that might affect what we do."

"When have you been doing all this?" Bob asks as he looks at his son in amazement.

"I haven't done it from the counter at 'Dunkin' Donuts," Jim responds, teasing his father.

"Dad, I really think we need to look at expanding our market. When we get back to the office I'd like to share with you Southeast's business report on new markets. I think you'll find it interesting. As great a job as you've done with Baker Pumps, there's room for us to expand our market. And the downside risk seems pretty small. I'd really like to know what you think," Jim tenders.

"I don't know," Bob hesitates. "I've got so much on my plate as it is."

"Perhaps this is an excellent example of Jim showing you an area he could handle, removing some of your burden," Bill observes. The trick is to find ways to give over things you are not as interested in doing that Jim can do. This eliminates the founder's dilemma of wanting to let go yet at the same time wanting to make sure the business continues on a successful path. What would it take for you to be confident that this new course of action has a good chance of succeeding, Bob?" Bill asks.

A smile comes over Bob's face, and as he breaks into a grin he says, "if it's my idea!" The room resounds with laughter as everyone joins Bob in laughing at himself.

"It sounds as if you're laughing at the Ol' Captain Bob," Bill grins. "What would the new Statesman Bob say about maximizing the risk of entering new markets?"

"Statesman, Bob," Bob replies, "says to do the same thing as before: look at a situation from every angle before making a decision. But Statesman Bob also says get others into the act. He still gets to decide, but his lieutenants can help gather helpful 'intelligence.'"

“So bringing this perspective to Jim’s recommendation, how do you assess his idea now?” Bill asks.

“I like the idea of involving the business school at the university. Their business school has a good reputation, and they could help us out, maybe even do a special study for us. The more I think about it, it seems Jim’s idea has real merit!” Bob concludes.

“Isn’t that a nice gift to you,” Bill says to Bob. “You decide to take on a new management approach by extending the net of information gathering to include Jim and a business school study. The result is potential market expansion for Baker Pumps and less stress and pressure on you: your family ends up laughing and you end up smiling. I call that real statesmanship!” Bob has a wide grin and the rest of the Baker clan are smiling as they learn along with him.

## **The Entrepreneur as Statesman**

Bill continues. “As a statesman, your decision-making will be of a different kind. Now rather than plunging in and making decisions yourself, in a problem-solving session you will be standing back to focus on the merits of the idea. You have the distance to make your considerations carefully while keeping the option of making the final decision yourself. As you begin to remove yourself from the role of direct manager and step up to that of statesman, you will be making decisions in a new way. You will have to evaluate ideas—not on who makes them and particularly not that they came from you or who is loyal to you—but on their merits for the company. You are ‘bracketing’ the source of the idea and evaluating its importance for the company. As you do that, you will find that ideas begin to flow from those below you at Baker Pumps. This creative energy can work for you in the business just as it’s working for you today at this retreat. What do you think about that?”

“I’m not quite sure,” Bob responds. “This is all new to me.”

“Maybe not as new as you think,” Bill suggests. “Let’s imagine a situation in which you’ve already done this in the business. Give me an example. How has it turned out?”

“Dad!” Jim chimes in. “That’s exactly what you did on Thursday with Tom and Sam. They each had ideas about the problem we were having with that intake control valve on the 409 pumps. You listened to both and actually took Sam’s advice—even though Tom and you are buddies.”

“Is that all you mean?” Bob asks Bill.

“Yes, that’s it,” Bill responds. “How did it work out for you?”

“Easy,” Bob replies. “That was nothing, no big deal.” “So changing over to a ‘new’ management style,” Bill concludes, “really isn’t so new and different after all. It just means doing more of what works and works well.”

“But, I’m still the boss,” Bob says, worrying about just where he’ll fit in.

“Of course you are,” Bill says. “And in a new management structure, you are still the boss. You’re just a different kind of boss. Superman is tired of saving the world himself, but in trying new things he doesn’t lose the courage that made him Superman. That courage is what enables him to take challenges to a new level he never imagined. What would be the first thing you imagine you will feel comfortable delegating to Jim that you haven’t yet done?”

“Fred mentioned something about benchmarks? A plan?” Bob queries. “I kind of liked that. But I guess I’ll need Jim’s help in implementing it. It would help to have something in black and white. I’d want to have confidence in Jim’s being a solid boss, that’s for sure. And I like the idea of Sam guiding him day in and day out. I just need to have both Jim and Sam report to me on a periodic basis on this concern. That would make it OK with me.”

“You’ve put your finger on exactly what a transition plan is,” Fred affirms. “It means that you let go of direct management control of Baker Pumps and in its place you implement a plan that phases you out and Jim in, on daily operations. You create a schedule of what things are handed over and by when. The easier things are first, the harder things come gradually. You can create a succession plan for whatever period of time suits you, Baker Pumps, and Jim. And maybe those professors at Southeast’s business school might have some ideas for you too. Their Family Business Institute has courses on succession planning. I’ve been to a few myself. I’ve got to think of the future of Fred Scott, P.A., too, you know.”

“I’m glad my alma mater is so up to date,” Bob says proudly. “Maybe they can be a resource to Bob Baker . . .,” chuckling to himself, “. . .formerly of Superman fame. I didn’t realize they could be of help to a small business. Do you really think they could help with a succession plan, Fred?”

“Yes, I do, Bob. They are educators. What they can contribute is information on how to go about it, solutions other businesses have tried, what’s worked, and so forth. In terms of creating a specific plan, Bill and I can help you with those details, based on what you learn at Southeast’s Family Business Institute. It’s a team approach. As a matter of fact, Bill and I can meet with you to discuss what the natural phases of succession are and what kind of a schedule would best meet the needs of Baker Pumps. Jim should be part of that discussion, and Joe could help too. We could have it for you before you and Jim get together to discuss assessing and retraining your managers to maximize his success.”

## **The Board of Directors’ Role**

“There are some other concerns you, Jim, and Bill should discuss as time goes on too,” says Fred. “This involves developing a business plan with goals and objectives and a schedule to match, say a five-year plan of your succession schedule—or whatever schedule you decide. It should also involve creating a capable outside board of directors with expertise in various areas to keep Baker Pumps on a stable growth plan. For instance, you might want to involve faculty

from University of the Southeast's business school.”

“I hate to have someone else telling me how to run my business,” Bob replies.

“I can understand that,” Fred responds, “but that’s not the role of a board of directors. A board is a policy-making body whose job it is to oversee the big picture, address long-range issues, and make strategic recommendations on the company’s future. Its job is not to micro-manage operations or get involved in day-to-day details.”

“That sounds more like a luxury than a necessity,” replies Bob.

“Not really,” Fred counters. “Look at where you are now. You want to step back from the business, yet have confidence in its successful continuity. We’re identifying resources that can help you accomplish that task. Creating a board of directors is a tool to help you achieve your goal.”

“Aw, Fred, you can handle anything for me that’ll be coming down the road, I’m sure,” Bob says with a bit of a furrowed brow and a frown.

“Not really, Bob,” Fred continues. “I’m just one part of your team, which now looks like that of Superman and Son. And none of us has a crystal ball. What if something, God forbid, happens to me. You would look for another qualified professional. Rest assured, I appreciate your confidence in me, Bob, but your professional advisors should remain advisors and not policymakers.”

“But what about my other advisors—my financial planner, my C.P.A. and my banker? You’re not all going down in the same plane accident, are you?” Bob queries.

“I certainly hope not,” Fred responds. “And we will need to involve each of them in finalizing your estate plan. But Baker Pumps, as they say, is bigger than both of us. Bob, you have a \$3 million business here, with many people depending on you. Keeping it running today is vastly different from getting it up and running thirty years ago. If his relationship with Southeast is any indicator, you have a great resource in Jim. He knows how to use advisors for immediate problems. But one purpose of a board of advisors is to develop a long-range business strategy. When was the last time you developed five- and ten-year goals for Baker Pumps, Bob?”

“You’ve got to be kidding,” Bob replies. “I’ve never had time for that.”

“You’ve been the fortunate recipient, then, of the old ABC’s, Bob,” interjects Bill. “Planning these days is a necessity to secure what you’ve been able to achieve.”

“ABC’s, what’s that?” Bob challenges.

“It’s three things—Ability, Breaks, and Courage,” Bill replies. “Most family businesses have succeeded because of these entrepreneurial factors. That’s great to this point. But it’s like being ahead 14-0 at the first half of an NFL football game, but with a full half more to play. You never know what’s going to come out of the locker room against you the second half.”

“Say no more,” Bob relents. “I understand. You two are saying I’m the coach with a great record, but every game is a new test. And it’s not over until it’s over.”

“I couldn’t have said it better myself,” Fred answers.

“To create a board,” Fred continues, “you would be chairman and CEO, Jim president and COO, and—in keeping with the tone of our discussion—Joe and Jane would be included as well. But you also need solid resources outside the family—board members who know your industry, who understand the market—and even those who can see how government regulation may impact your business.”

“I draw a blank there,” Bob responds. “No one comes to mind to fill that role.”

“Dr. Gutierrez from the university would be a good candidate,” Jim suggests. “He certainly is an expert on market trends.”

“I’d have to meet him,” Bob replies, “but that makes sense. I don’t know where else to turn, however.”

“You don’t have to make your decisions on the spot,” Fred cautions. “The make up of a board is a very important task.”

“When you talk about the industry expertise needed,” Bob goes on, “the people who know the world of marine pumps best are my direct competition.”

“That’s quite common,” Fred acknowledges. “Sometimes companies have to go outside their regional market to draw upon qualified experts who are not in competition with them. Your trade association, the National Pump Association, may have resources for you as well,” Fred offers. “Since this is a major decision, why don’t we put this item on our list for discussion after the retreat so we can move on to other concerns.”

“That sounds fine to me,” Bob concludes.

## **Confirming Management Succession**

“Let’s wrap up this portion of our agenda by going back to your list of successful succession needs,” Fred suggests, going back to the flip chart. “The Baker Successful Successor List has on it . . .

1. **Takes** charge
2. **Cares**, has a sense of ownership
3. **Good** technical manager
4. **Tough** manager

5. *Has* market savvy
6. *Understands* operations and sales.”

“We’ve seen how Jim has a take-charge attitude toward the business by the initiative he has shown toward you, Bob. Is that fair to say?” Fred says looking in Bob’s direction.

“Sure is,” Bob replies.

“Certainly in his sharing of insights on personnel in the firm, in coming up with new marketing ideas, and in persevering in his opinions in discussion with Bob. I would also say those same traits express that Jim certainly cares about the business, and he is involved in it with a sense of ownership and personal commitment to make it succeed. Do we have a consensus on that?” Fred asks as he scans the room. Everyone nods in unison.

“In terms of technical management, Bob said he believed Jim may not understand the manufacturing as deeply as he might wish, but what was interesting were the comments about how Jim is instinctively good at building teams and utilizing the wisdom of the mechanics and engineers at Baker Pumps. This really is a unique skill, and Jim seems well-suited for a future in which team building is a great asset,” Fred suggests.

“It’s different from how I manage, but if it works for Jim, hey that’s great,” Bob replies. “Jim may not have the engineering background I have, but he is able to motivate people in a way that I don’t naturally do. So I’m not worried about the technical side of things.”

“‘Tough manager’—that was a big concern of yours, Bob. How do you see Jim in this regard now?” Fred continues.

“Well, he has an eye for problem employees, but I’m still not sure he knows what to do about them. I like the idea of having Sam McCall help him in this area. Sam has real street savvy that I think Jim can learn a lot from. And the two of them have a solid relationship, so I think that has great potential. And I’m not knocking you, Jim, I just think Sam can be a big help to you in this one area,” Bob says looking at Jim.

“I know, Dad,” Jim replies. “I don’t take it as personal criticism. I never learned the old-style boss authority that is second nature to you. And that’s not really me, either. But I can see that at crucial times, someone needs to clearly make stands, and perhaps say ‘no’ over an unpopular issue and be decisive.”

“It’s important to remember once again,” Fred stresses, “that there are employees who will be unable to keep up with the demands of a growing business. After a certain point, the business outgrows their capabilities. This is a reality that needs to be anticipated. Otherwise, such employees will end up resentful about being left out or feel over their heads, leaving a serious personnel and morale problem. This is also true, I hate to say, Bob, of owners too. Baker Pumps has challenged your capabilities as you move toward retirement. You don’t have the same



stamina as you did thirty years ago. And while this doesn't mean you should be put out to pasture," Fred continues, "it does go to show that just as your motivation is responding to the growth of Baker Pumps, you will have employees who are responding in a similar fashion as well."

"I admit you're right, Fred," Bob acknowledges. "Let this be a reminder, Jim, that management is a never-ending job. Just when you think you've got one aspect of the business under control, another part pops up demanding your attention and challenging your wits. I guess I'm not as enthusiastic about testing myself with those challenges as I use to be."

"That's a big admission, Bob," Fred responds. "There are many founders who never are willing to step back and pass the torch along like you are. Your ability to look at your situation and yourself objectively is a great asset. And it is key, I think, to how profitable our discussions have been today." Bob grins a bit sheepishly but takes in Fred's compliment.

"Let's move on to the area of 'market savvy' on the succession list now," Fred suggests.

"How surprised are you at the evidence of Jim's capabilities shown here today?" Fred asks.

"He's got savvy that I never knew he had," Bob replies. "I like that. I don't know if entering foreign markets will be the way to go, but I can consider that it might have great potential. What has really become clear to me today—and that discussion really brought it home—is that Jim is really an indispensable part of the business management already. He's already integral to the operation in a way I just hadn't seen. Getting a little distance from work has helped me see just how significant a role he already has in Baker Pumps. With all the criteria up there and with us covering all of them in the discussion, why that's great. But my greatest reaction is a sense of confidence in Jim's ability and in having him as my successor at Baker Pumps."

"That's great, Bob. What a nice sense of satisfaction and accomplishment that must be for you. And for you, too, Jim, to have your Dad's vote of confidence as Baker Pumps enters a period of succession. I'm sure everyone else here shares some of that sense of accomplishment and satisfaction," Fred offers as he looks around the room.

Everyone is smiling and nodding approval. "I think this is great for both Dad and Jim," Joe offers. "As you said in the beginning, Fred, a transfer of Baker Pumps can be a pretty worrisome time. And there seemed to be so much that was uncertain. But now, the foundation of everything seems to have fallen into place. And I want to again offer my help, Dad, with that accounting package and in any other way I can support the business."

"Joe, you're a master of timing," Fred notes, "because 'Operations and Sales' is the last item on the list. What's your assessment in this area, Bob?" Fred inquires.

"It would be great to have Joe's input and advice. General ledger, taxes, and even tax planning have been an on and off nightmare over the years. I'd really like to get a handle on that. Maybe Jim is the person you should talk to now, Joe" as Bob gestures to Jim next to him and puts a hand on his shoulder.

“And I want to count on Jane’s help, too,” Jim responds, “perhaps as office manager. She has a good overall view of the office, knows accounting, and the employees trust her. What do you think, Jane?”

Why, that might really work out,” Jane reflects. “What do you think, Jeff?”

“I’ve never seen you so excited,” Jeff comments in an unusual gesture of support. To everyone’s surprise, he continues. “That tells me this idea has good possibilities. We might have to make after school child-care arrangements; that’s the first thing I think of.”

“Anticipation is one of the best problem-solving skills a person can have,” Bill Smith observes. “If Jane changes her work commitments and schedule, you and the children will certainly be impacted, Jeff. You’re smart to start thinking about options right away.” Jeff is as surprised by the recognition as Jane is by his positive involvement in the discussion.

## **Tying Up Loose Ends**

“Before we take a break,” Fred adds, “I want to note that we will have to set a time to complete the loose ends of today’s discussion. Checking his legal pad, he says, “let’s see, so far I have listed—

### **Follow-Up List**

1. Develop a time frame for a succession plan with clear benchmarks, including an employment contract for Sam McCall.
2. Have Joe prepare information about a new computerized accounting system, and discuss Jane’s role in its implementation.
3. Develop a candidate list for a board of directors, including prospects from the National Pump Association as well as Dr. Gutierrez from the University of the Southeast.
4. Discuss ways the University of the Southeast might help with some market studies and possible business-succession courses for Bob and Jim.

“Is there anything I’ve missed?” he asks as he looks around the group. Receiving no response, he assigns one or two people to be responsible for each item on the agenda. “I’ll have my assistant type up the agenda and send a copy to each of you,” he says. “When you get it, I’ll have her call to work out when you are available for a meeting. Could you ‘attend’ via conference call, Joe?” Fred asks.

“Yes, that will be best for me,” he replies. “I’ll send the accounting information down day

after tomorrow so everyone can have it prior to the meeting.”

“OK, then let’s all take a break, and we’ll come back and talk about the estate-plan portion of our agenda.”

And so the outlines of a successful management-succession plan for Baker Pumps is agreed on and the transition has begun. The immediate worries that brought Bob and Sue into Fred Scott’s office were, at the core, relational ones—family concerns that were inseparable from business concerns. For the Bakers to have peace of mind about their estate, however, additional issues will have to be addressed. They want to make provision for all their children in their estate, and the grandchildren too. And they have assets other than business assets for which they need to plan and include in their retirement.

## Reflections

1. The Baker family retreat directly addresses issues that, if left open, would surely create difficulties for Bob and Sue’s plan. The Bakers, of course, could plan their estate without a retreat; but because the business is a family business, they decided to involve everyone in their search for solutions. Their initial concern—that their family was somehow “different” because it had “problems”—melts away as they see these issues are readily solved. By exploring strengths and talents, it becomes apparent that Jim is not “immature,” and Joe is not “alienated.” Jane has capabilities to contribute to the business in spite of her marital difficulties. In addition, Bob and Sue feel much better about themselves as parents compared to when they began to examine their family worries. The family retreat opens communication lines to give each participant the chance to see themselves and their family in a more empowered fashion, and hopefully to see the future of Baker Pumps in light of emerging opportunity. The retreat ends up being an opportunity for bringing the family together rather than cementing a sense of alienation. And contrary to their concern that the retreat will lead to a loss of control over the succession process, Bob and Sue find they have a greater degree of control through the widespread and positive participation of their children.

2. The retreat also provides Bob the chance to see the big picture for his business. His daily preoccupation with phones, customer complaints, and vendor problems and the demands of an everyday hectic schedule all shield him from more clearly seeing the future. Planning needs to be done in a setting conducive to reflection. While the Bakers’ Keys vacation home provides this, a variety of other settings could have met the same objective.

3. The focus of a retreat is always solution-oriented. This means several things. Most importantly, the tone is always positive. The assumption is that all are there to find solutions and new ways of handling current difficulties. This is done by reading between the lines —listening to the strengths and resources and talents evidenced, but not clearly defined. It is the role of the professional to glean these underlying abilities from the fodder of the discussion and bring them to everyone’s attention, weaving them into the subject matter at hand. If the focus was on

“problems” alone, it would be easy to get bogged down in them.

4. The discussion is tightly focused. Having an agenda to begin with sends a clear message to all participants that the facilitators mean business and that the business of the retreat is clearly the succession of Baker Pumps and Bob and Sue’s estate plan. Bill Smith and Fred Scott keep the discussion channeled to these issues. When disagreement occurs among the participants, the facilitators do not let it become personal, but keep to the (business) topic at hand. This is a distinction participants understand very easily. Also in a group setting, on occasion one person can dominate the discussion. Bill and Fred do not let this happen. Further, through Bill and Fred’s style of listening and leading, wide and open participation is encouraged and, as a result, various family members actively participate in the discussion.

5. Solutions can come from anyone and everyone. Jim and his Dad might seem to be the primary figures in a discussion of management succession, but the discussion and ideas for solutions will come from anyone. The facilitators’ job is to keep channels of communication open, urge hesitant participants to speak, and affirm new solutions and solutions that have worked for the family before and/or ones that may already be at work in this discussion whether or not participants are aware they are using them.

6. The retreat discussion is neither counseling nor psychotherapy. It is a focused and positive discussion with wide participation oriented to finding solutions to current business dilemmas. Intense feelings emerge from time to time and differences are aired, but the focus is not on personal feelings, individual insight, or past family history. Resolution in these areas may occur as a result of the discussion and if so this is a bonus rather than a goal or focus of the retreat which always remains the development of the succession plan.

7. In seeing the big picture, Bob also gets a glimpse of the challenges of the future. He and/or Jim will need a trusted core of advisors—both professionals and a qualified board of directors. And having business and succession plans in place—as changeable as they will be over the near and long term—will provide a sense of control for Bob that he previously got from exerting direct influence on the daily operations of the business.

## Chapter 5

### ESTATE PLANNING:

## Sculpting a Legacy from Business and Family Needs

### A Legacy Rooted in Caring

Bill Smith reconvenes the Baker clan to begin discussion of a different but related topic, that of Bob and Sue's estate plan. The basics of the business-management succession have been achieved, enabling the group to move on to subsequent issues.

"A concern of most every individual and couple I've worked with," Bill Smith begins, "is how to provide for their family after they're gone. If there are no children, people are concerned about other family members. But more often than not they are parents who have children and/or grandchildren. While no one likes to think about dying, one of the most important stages of adult life is the last one. Psychologist Erik Erikson calls it 'Integrity versus Despair'. This simply means that older adults do not have their own future to look forward to anymore; so they look to the past—to their own accomplishments and failures, their dreams and frustrations—to assess their accomplishments and life. They also look to those they care about and invest emotionally in *their* futures. The successful resolution of this psycho-social task brings a new sense of self, of pride in their lives and a certain humility knowing that, although they have not been perfect, they have done the best they could, limitations and all."

"That certainly sounds like Mom and Dad," Jane observes.

"They impress me that way too, Jane," Bill expands, making eye contact with Bob and Sue. "And I would guess that's for two reasons. One is that they love and care for one another; and I believe that's apparent to everyone in this room, even to family outsiders like Fred and me. They have remained together through all the ups and downs of their life, raising a family, and creating a successful business enterprise."

"The second thing that I see," Bill continues, "is that they care for their children and for their children's future. In some fashion they will have a future even after both are gone because they have a family to continue not only their name, but more important, their values and philosophy of life."

"But what about people who don't have children?" Joe asks. "They won't have a 'future' beyond themselves."

“Actually many couples—and individuals for that matter—live very fulfilling lives without children. They make commitments that transcend their own lives and create a legacy that outlives them. This may be through a social cause, or through a charitable organization, or through some purpose they are devoted to. Some set up scholarships for special groups of students at their favorite universities. Others create private family foundations with endowments that perpetuate their own social values such as preserving the environment. In any case there are a number of ways people can affirm the future of humankind beyond their own time on this earth.”

“Couples with immediate or extended family whom they care about face the challenge of how to distribute their possessions and assets. This is a challenge for Bob and Sue since their biggest asset by far is Baker Pumps.”

## **Issues of Fairness**

“While most families,” Bill continues, “want to treat their adult children equally, when the family business is a major asset, this is not always simple. In the name of fairness, some families restructure their corporations in such a fashion that the children will not end up competing or struggling against each other in the same business. For example, the corporation might restructure itself through a spinoff or split off, so one or more children would ultimately own and operate separate corporate entities so as to minimize conflict. In many cases, corporations have developed new product lines to facilitate separate management by different children. Another alternative is to give the business primarily to one child who becomes the successor manager and eventually the owner and then to compensate the other adult children in some rough fashion. Professionals refer to this approach as ‘rough justice.’”

“Or in some families, each child thinks of the family business as his or hers. It often happens that when the founder passes on, the business ultimately gets torn apart, can’t keep up with its competition, and ultimately gets sold out to the highest bidder at a fraction of its worth. This leaves the spouse and all of the adult children with a small portion of what they otherwise would have had if the business had prospered under single management. This is a reality everyone in this room needs to understand. And if there are concerns about having any child as the major stakeholder, we should discuss them now. There are other options, one of which is selling the business, that can be considered.”

“Don’t we all assume that Jim will now be running the company if Mom and Dad’s succession plan works out?” Joe asks. “I don’t have a problem with that.”

“I don’t either,” Jane comments. But no sooner than the words come out of her mouth, however, she receives a hard nudge in the ribs from her husband. She glares at him, and he looks away.

“You know,” Bill Smith responds taking a cue from Jeff’s gesture, “we haven’t heard much from the in-laws yet today. That’s perhaps natural since the discussion of Baker Pumps

management doesn't directly concern you. But making Jim Bob's successor is the root of a set of decisions that will affect everyone in this room, whether they have a part in the management of Baker Pumps or not. And I expect Jennifer, Jill, and Jeff wonder just how the Baker estate plan will affect them and their children." Jennifer and Jill nod in agreement. Jeff doesn't say anything but sits up in his chair and leans forward as if to learn more. "Fred will now go into the details of estate planning," Bill says as he sits down.

"From Bob and Sue's estate-planning perspective," Fred begins, "Baker Pumps is their central asset. If Jim is to be Bob's successor, then certain other things flow from that decision. I'll explain in a moment, but if we assume for now that Jim and his family will ultimately receive or control the business assets, where does that leave Joe's and Jane's families? Furthermore, good estate planning in a family with assets such as Bob and Sue's will involve not only the next generation of their children, but the third generation as well. And since Joe and Jennifer have one child but Jane and Jeff have three, how can Bob and Sue distribute their assets in a way that is fair to all? Is that a fair statement, Bob and Sue, of the concerns you have?" Fred asks. They nod in agreement.

"You all need to know that when it comes to estate planning," Fred continues, "and to the distribution of diverse assets, there is no such thing as perfect justice. Accommodations to reality must be made. Jim may inherit Baker Pumps and thereby from all appearance receive a greater inheritance. But given the risks associated with small businesses, what might appear to be a great inheritance for Jim could actually turn out to be less. Add on the headaches of operating a business, which are absent from inheriting other types of assets, and you can see how the calculations of 'rough justice' begin to work."

"It's advantageous that Bob and Sue have other assets to work with—this beautiful vacation home, Bob's IRA, their investments, and insurance possibilities as well. We will discuss these in more detail shortly, but at this point the most important things are that they know their parents want to take care of them and their families and that Joe and Jane are comfortable with Jim's having a major stake in Baker Pumps."

"And let me add a point about the delicate position of having married into the Baker family," Bob shifts, looking directly at Jill, Jennifer, and Jeff. "In-laws are not in a blood line of succession to a family's assets. The families into which in-laws marry may feel obligated to their children, but will naturally not feel obligated to those their children have married. At the same time, in-law spouses are often parents to the grandchildren who are in the family lineage. From past experience, I've found that things work best when in-laws do not worry about their own individual interests but orient themselves to what is best for their children. I say this because when estate plans fail it is often because someone believes they are entitled to benefits or opportunities that the testators have not provided. This can lead to open family conflict, court battles, and ultimately even the depletion or entire loss of family assets and everyone loses—all over misunderstanding about entitlements. In-laws may have their own families whose estates will be inherited someday. While any such assets may not be equal to the family into which they married, and as much as we might like it to be different, life is not guaranteed to be equal or fair.

For some this realization is a bitter pill to swallow, while for others, its simple wisdom makes life much easier. A bit later we will talk about the distribution of other Baker assets and ‘rough justice’ in light of Baker Pumps being transferred to Jim. Does anyone have questions at this point?”

There is a silence as Jill, Jennifer, and Jeff still wonder what this really means for them. Then Bob speaks. “I do like the plan to have Jim as my successor. We may have some rocky times, but I believe 5 years or so will give us time to make a solid transition. Baker Pumps has been my life, and (gesturing to Joe, Jim, and Jane) it is your mother’s and my legacy to you. And as much personal satisfaction as I get from being the head of Baker Pumps, I am realizing it’s time to pass this business along in a form that benefits all of us. But if anyone has any reservations, I’d rather have them voiced now before your Mother and I make a final plan.” Everyone sits in silence—including Jeff—eager to hear about the next step.

“That’s great,” Fred concludes. “I give you all credit for openly and directly addressing these crucial issues. Everyone here has an investment in Baker Pumps—both emotional and financial—since you all share in the Baker legacy. “Estate planning,” Fred continues, “is an involved enterprise. For the Baker legacy to continue, a plan needs to be implemented that will serve as Bob and Sue’s voice after they both are gone. Because of the variety of their assets, this plan will be fairly complex. Special arrangements will need to be made for each asset. While not everything will be exactly equal since the assets are like a basket of apples, oranges, and bananas, Bob and Sue do need the reactions of the rest of you to get some ideas so they can create the best and most effective long-range plan possible.”

## **Family Relationships and Family Legacy**

“Bob and Sue, will you share some of your own goals concerning the children and grandchildren? And your thoughts and feelings about what it means to be creating a Baker family legacy?” Fred asks.

“I’m proud just to be here today,” Bob begins. “I have my entire family and my wife of 40 years with me, and I feel extremely fortunate. Baker Pumps has meant everything to me in the past, but now I see it as a lever to a new future for Sue and me. Our kids and their futures now mean the most to me, and I want to have a healthy future in which I can enjoy my children, their spouses, and my grandchildren in a way I haven’t before.”

“How about you, Sue?” Fred asks.

“I love my children and grandchildren too. I understand what you say, Fred, about in-law problems. But I feel Jill, Jennifer, and Jeff are very much a part of our family, and I want what is best for everyone in the room” (nodding to everyone around the room).



“That’s beautifully said, Sue,” Fred affirms. “And one of the reasons, I recall, that you and Bob wanted to have this retreat was to develop a plan that’s best for everyone. Our challenge is how to make this happen practically.”

“Bob and I don’t know how to work out all the details,” Sue continues, “and that’s what we look to you and Bill to help us with. I also worry sometimes about the future, and I don’t want to happen to our family what has happened to so many who end up in squabbles over their parents’ estate as soon as they’re gone.”

“Do you have a specific concern?” Bill Smith asks Sue.

“Well, to be honest, I do,” Sue responds. “Bob and I were worried a bit about each of our children. Parents are entitled to worry, I guess. We were worried about Joe’s distance from the family, about Jim’s ability to succeed Bob, and, I have to say this Jane, about the stability of your and Jeff’s marriage. I’m not making any judgments, but as Fred tells us over and over the key to effective estate planning is the strength of the relationships among the people concerned.”

There is a moment of silence, and then Jane replies. “I was concerned that my marriage would come up in the discussion this weekend,” she says.

“I told you we shouldn’t have come!” Jeff accuses.

Bill Smith intervenes to take charge. “Jeff and Jane, no one is here to make judgments about your relationship or anyone else’s. All of us in this room have had low as well as high points in our marriages. Is that fair to say, everyone?” Everyone nods in agreement. “If you two are having difficulties right now, I believe you have the potential to solve them. At the same time we all know the high divorce rate in America and that many couples choose divorce as their solution. The goal today is not to get involved in your marriage but to help Bob and Sue make a long-term estate plan that takes realistic account of relationships as they are today, always with the hope of a positive tomorrow.”

“You mean we’re not going to be put on the hot seat?” Jeff asks with a mixture of defensiveness and relief.

“The goal here is planning for three generations,” Bill responds. “And there are ways for Bob and Sue to take account in their planning of your current marital situation without making any presumptions about how you and Jane will work things out,” Bill reassures him.

“What do you mean?” Jeff asks curiously.

## **Protective Trusts**

“There are arrangements called protective trusts,” Fred begins. “They protect the interests of a beneficiary—most often an adult child such as Jane—and make certain the wishes of the legators—typically the parents—will be carried out. The parents are in the natural position of

wanting their adult child to receive her inheritance, and if she and her spouse divorce, to make certain she retains her inheritance. This is only natural since the daughter and her children are part of the same kinship line. The same consideration would hold, for instance, if something were to happen to Jeff, and Jane would be left alone to raise her children. In families with marital stress, some spouses seek divorce as the best solution. In that instance, the dilemma is how to shield one spouse from any debts he or she was not responsible for originating. A common example is when two spouses hold credit cards in their separate names. Clearly those debts belong to the respective spouse. The spouse with the inheritance would not be responsible for her partner's individual debts. Her family would be assured, consequently, that the inheritance would be protected for her and her children's use."

"Sometimes," Fred continues, "couples who are not considering divorce prefer to keep their finances separate. One may have a business with liabilities the other does not wish to share. Or they may each value their independence and want to keep separate checking, savings, and investment accounts. Jeff and Jane, for instance, might want to discuss the advantages and disadvantages of having separate finances."

Joe speaks up. "That brings up concerns for all of us," he begins. "I worry from time to time that if I were to die suddenly, Jill wouldn't have the capability of managing the funds she would end up with. We have the baby, and I'm concerned about him too. Jill is a great mother and would raise him in fine fashion, but she doesn't have experience managing money. She didn't grow up with money, and in our marriage I've been the one who's managed it. I'm not speaking about just minding expenses, but having a solid financial plan, investing, etc. If I died today, Jill would be very well off, but I'd hate to see her have heavy financial responsibilities and be on her own with no help."

"I'm touched with what you're saying, Joe," Jill replies. "I've never given any thought to what you're saying, but it makes sense. You've always taken care of the budget, and we've always had enough money. But I never thought of having a lot of money and never thought of having it without you. I have no idea what I'd do other than be very sad."

"Is there some kind of protective trust that applies to our situation, too, Fred?" Joe asks. "As I told you at the break, Jill and I have done some estate planning of our own. Our attorney mentioned that possibly you could save our child some estate taxes by placing some or all of my possible inheritance in a generation skipping trust?"

"That's a good point, Joe," Fred responds. "Your situation isn't unusual. A trust can be designed to protect Jill as well as avoid taxes at your death. We will discuss generation skipping trusts shortly, which may be the way to achieve your goals. You should know, too, that there are trust officers from your financial institution who can be extremely helpful in managing such a situation."

"But," Fred says, returning to his focus, "we need to keep the horse before the cart. And that has to do with how Bob and Sue, in light of Jim's inheritance, can equalize gifts to you and Jane, so let's move onto that discussion now."

“Before we do,” Sue interjects, “I want to say how proud I am that Joe shows his love for Jill in this very touching way.” “Perhaps he’s showing the same love for his family that you and Bob have in planning for the future the way you have,” Bill observes.

## **Family Limited Partnerships**

“Since Bob and Sue want to equalize their gifts to the three adult children,” Fred continues, “one of the assets they have to consider is the commercial building that houses Baker Pumps. Bob and Sue own the building as tenants by entirety, and they lease it to the corporation. I recommend that Bob and Sue create a limited partnership with Bob and Sue as shareholders of a new “S” corporation that will be the general partner. They will also own all of the limited partnership interests to begin with, but over time these limited partnership interests will be transferred to trusts created for Jane, Joe, and possibly the grandchildren. The commercial building is transferred to the partnership and a long term lease is entered into between the partnership and Baker Pumps.”

Fred continues, “The goal to be accomplished through this method of gifting is that the gifts of limited partnership interests will be covered under the gift-tax annual exclusion and so will be excluded from Bob’s and Sue’s estates. Additionally, the gradual gifts of the limited partnership interests should be subject to what is called a ‘valuation discount.’ This is a provision that applies to the limited partnership interests when they are given and also to the far off future when Bob and Sue die, because presumably at that time they will hold minority interests in the partnership, and these interests will have a discounted value because of that.”

“I’m not sure I follow all that,” Joe queries.

“Me neither,” Jane concurs.

“The family limited partnership is simply a way for your parents to transfer to you the building that houses Baker Pumps. Legally it is not part of the business, so is not part of the business interest Jim would inherit. And since a building cannot be carved up room by room and distributed, the use of limited partnership interests accomplishes what amounts to the same thing. And it is done,” Fred explains, “in a way to minimize the tax on transferring this asset to you two.”

“Hey, that’s pretty clear,” Jim confirms.

“How about the rest of you?” Fred asks. “Am I keeping you with me?” He gets affirmative nods from around the room.

## **Value Shifting through Gifting**

Fred then introduces a new area, one he calls “value shifting.” “An important consideration for a family transferring assets across one or more generations is that of value shifting,” he

begins. “Its purpose is to presently shift a valued asset with potential for appreciation out of a taxpayer’s estate to that of a younger taxpayer who also will have time in life for the asset to appreciate in value at lower rates. Consequently, I recommend a plan to Bob and Sue that you each start using your \$13,000 annual exclusion gifts immediately for both the children and grandchildren. Gifts of stock in Baker Pumps would be made annually by both Bob and Sue to Jim and his children, with the remaining stock to be transferred to Jim upon the last to die of Bob and Sue. Annual gifts would also be made by Bob and Sue for Jane and Joe, with their gifts being made to trusts that would be established. In order to qualify under the \$13,000 annual exclusion permitted by the Internal Revenue Code, these trusts must be structured to contain certain withdrawal rights commonly referred to as ‘Crummey rights of withdrawal.’ The word ‘Crummey’ comes from a famous tax case involving a taxpayer by that name. Basically, if the trust beneficiary has the right for a limited period of time to withdraw a contribution to a trust, then the gift to the trust will qualify for the annual exclusion. The detailed mechanics of Crummey trusts are beyond the scope of the retreat, but,” Fred notes, “it is important that the trusts set up for Jane and Joe contain Crummey rights of withdrawals for the beneficiaries so that annual gifts will qualify for the annual \$13,000 exclusion. Also, it is important to note that with regard to trusts for grandchildren, these must be separate trusts for each grandchild.”

Fred suggests that Bob and Sue follow this plan and that \$13,000 annual gifts be made to each grandchild via trust by both Bob and Sue on an annual basis. These trusts can provide that principal and income distributions be delayed until the grandchildren are at an age where they can properly manage their own assets. Fred pulls some figures out of his briefcase showing the tremendous benefit of value shifting by making these annual exclusion gifts for many years and how great the tax savings will be. “For example, a 60-year-old person and his spouse (the donors) who have three children and six grandchildren could give \$13,000 each year to each child and each of six grandchildren (all being the donees). This would remove a total of \$234,000 from the donors’ estates each year. A 60-year-old person has a life expectancy of about 24 years. If the donors were to make these gifts every year for 24 years, they would have transferred approximately \$5,616,000 (and the future appreciation on that \$5,616,000) from their taxable estate to their children and grandchildren. At first glance, a gift of \$13,000 to each donee may seem like too small of an amount to make any difference in a large estate. However, compounded over many years, the value shifting results can be impressive

Fred explains that the donor need not be committed to making these gifts each year for life but can choose each year whether to do so or not. The donor can make the gift outright to the donee or can set up a trust for the donee’s benefit and in the trust state at what ages and in what amounts the donee can reach his or her funds. This works especially well when minor children or grandchildren are involved or the donor is concerned that the donee will waste the money. The donor could also choose to set up an account under the Uniform Gifts to Minors Act or Uniform Transfers to Minors Act. However, most state laws require that the funds in these accounts be transferred to the minor upon reaching age 18 or 21, and often the donor is concerned that the donee is too young at this age to make good investment decisions.

Fred also remarks that the donor can make these annual exclusion gifts using a variety of different assets. Cash, publicly traded stocks, and mutual funds work very well because they are all relatively easy to transfer and easy to value. Fred reiterates the purpose of value shifting—to presently shift a valued asset with potential for appreciation out of a taxpayer’s estate to that of a younger taxpayer to avoid estate tax on the gift and its appreciation. As this is a present gift, the donor must be comfortable with giving up all control over the asset gifted.

For gifting purposes, Fred suggests that Bob and Sue open accounts in trust through their financial planner, Susan Jones, to be established for Joe and Jane and their children. He further recommends that Susan continue the excellent program of investing that she has been doing for Bob and Sue. Remember that his investment program has produced total annual returns in excess of 6% each year for the last several years. The annual exclusion gifts to Jim and his family will be in the form of stock in Baker Pumps, Inc., using a discounted value for each share of stock given, given that the stock will be a minority interest and non-marketable in the hands of the recipient.

## **Stockholder’s Agreements**

Fred also recommends to the Bakers that Baker Pumps, Inc., establish restrictions contained in shareholder agreements that will provide for any selling shareholder to offer his or her shares first back to the corporation or to other shareholders at an agreed-upon selling price. This should also provide for the mandatory sale by the shareholder back to the corporation in the event of an involuntary transfer such as a divorce or bankruptcy proceeding. Also buy-back provisions will be exercised upon the death or disability of the shareholder. These restrictions are necessary in order to preserve the ownership of stock within the Baker family.

## **Valuation Discounts**

Fred continues the discussion of gifting by introducing the idea of valuation discounts. “There is a substantial advantage, Bob and Sue,” he continues, “to making periodic gifts of corporate stock to Jim and his children. In Revenue Ruling 93-12, the IRS announced that notwithstanding the family relationship of the donor and donee and other shareholders, the shares of other family members will not be aggregated with the transferred shares to determine whether the transferee’s shares should be valued as part of a controlling interest.”

“What does that all mean in our case?” Bob asks.

“It means that a discount for a minority share in a business is available,” Fred explains. “This is because small blocks of stock cannot control the operations of the business—such as setting compensation, appointing directors, selecting business contracts, liquidating or dissolving the corporation, paying dividends, and other such decisions. In effect, the inability to exercise or control corporate decisions results in a deduction of value in the shares owned.”

“That’s good, right?” Bob wonders.

“Yes it is, Bob,” Fred replies. “It means that while the recipient of the stock receives full value for minority shares, the IRS allows discounts in the value of the stock for gifting purposes. In addition, there is a discount for lack of marketability. The IRS recognizes this because in the case of Baker Pumps, Inc., there is no established market for the shares compared to those you would find, for instance, for a corporation traded on the New York Stock exchange. The total discounts for minority and marketability can be substantial. This means that the amount of stock in Baker Pumps you can transfer to Jim and his children increases while keeping the gift tax to a minimum or nothing at all.”

“Keep up this discussion,” Bob says. “I like this no- to low-tax talk a lot!”

“You do need to know that at each time the stock transfers are made,” Fred continues, “it will be necessary to obtain an appraisal of the business. At that time the appraiser will appraise the corporation in its entirety and will establish the value of the minority shares being given, including the appropriate discount for minority and marketability.”

## **Providing Liquidity Through Life Insurance**

“Our discussion on these past sections has been technical,” Fred acknowledges. “But that is because Bob and Sue’s prime asset is Baker Pumps; and in order to achieve their goal of transferring assets to their children and grandchildren, certain rules and regulations must be followed. So we have discussed ideas of gifting corporate stock, the stockholder agreements that support such a move, and the area of minority discounting, which enables Bob and Sue to maximize their gifting according to law.”

“There are other areas of opportunity, however, which can help Bob and Sue achieve their goals—insurance is one of them.”

“One of the reasons small businesses rarely pass to the next generation,” Fred continues, “is that the business owner fails to adequately provide for payment of estate taxes. Normally, because of the unlimited marital deduction, there are no estate taxes payable upon the death of the first spouse. However, when the second spouse dies the estate tax bite can be considerable. Remember that, as of 2012, the tax rate for all assets in excess of \$5.0 million is 35%. Therefore, Bob and Sue,” Fred goes on, “you are facing a marginal estate tax rate of 35% upon the death of the second spouse, and possibly even as high as 55% if congress makes no changes prior to 2013. One major goal is to provide sufficient liquidity so that assets do not need to be sold upon the last spouse’s death. This is one of the places where life insurance comes in. If life insurance is used in the proper way, then a subsequent goal of avoiding paying estate tax on the life insurance proceeds may also be achieved.”

“You’re speaking my language, again, Fred,” Bob chimes in. “But how can you avoid taxes on money you receive from life insurance,” he asks.

“There are basically two ways,” Fred answers. “The first is to have the beneficiary purchase the life insurance as owner and beneficiary. This means that you and Sue would not own the policies on your own lives. The second is to purchase the life insurance through an irrevocable life insurance trust,” Fred explains.

“I recommend that you, Jim, purchase a ‘second-to-die’ life insurance policy on your parents’ lives. This will cover your allocable share of estate tax on Baker Pumps.” “You should understand,” Fred goes on, “that the amount of the actual insurance purchased will be calculated not only on the current fair market value of the business but will also factor in growth of the business.

We hope there will be little future growth of assets in Bob and Sue’s estates as a result of the value shifting we discussed earlier.”

“I see what you mean,” Jim adds. “I always thought insurance was a luxury, but now I see it’s a necessity for what Mom and Dad want to accomplish. Jennifer, we’d better take a look at our estate plan to see where insurance fits in, too. I’m getting some great ideas, Fred. Thanks a lot!”

“You’re welcome, Jim. You’re right to think about insurance for yourself, because in the event you die prematurely, your own estate plan will need liquidity, and insurance may enable you to pass the family business on to the next generation just as your parents are doing. Even more so, a second-to-die policy would be considerably cheaper now, than if you wait thirty years as your father has done.”

“That makes a lot of sense,” Bob and Jim say simultaneously, and then laugh together. The rest of the family laughs along with them, delighting in seeing two generations of Baker businessmen share a spontaneous moment. Fred and Bill join in the laughter, and then Fred continues.

“You should know that there are alternatives to buying life insurance for the business. Assets can be sold to pay the estate taxes; but at least for Jim, this is not a feasible alternative with respect to the corporate stock. Jim could also borrow against his corporate stock, but this may strap the business significantly at a time when cash may be needed for corporate purposes. Another method for paying the estate tax is in installments under Section 6166 of the IRS Code. In order to take advantage of the law—which provides for interest-only payments for the first four years, with principal and interest payments then amortized over 10 more years—it is necessary that the business constitutes 35% or more of the adjusted gross estate. Here again this type of borrowing may severely restrict the opportunities for the business.”

“It sounds as if I could really have my hands tied in running the business after Dad and Mom die,” Jim observes. “I’ll be busy enough as it is trying to build upon the success Dad has already created. I can’t imagine being distracted by these estate worries.”

“That’s exactly the benefit of a life insurance plan, Jim,” Fred replies. “Life insurance has an important role in a multi-generational estate plan.”

## Other Roles for Insurance

“In a similar vein,” Fred continues, “insurance can play other important roles in the succession plan for Baker Pumps.

“I hope we’re talking about saving money, not spending more of it,” Bob says cautiously.

“Insurance can be a helpful if it is used wisely,” Fred responds.

“What are you thinking of?” Bob persists.

“Thinking of Baker Pumps first and foremost,” Fred explains, “the company is in a vulnerable position during this period of transition. You should consider key man life insurance too.”

Jane immediately turns her head and eyes Fred. “Don’t you mean key *person* insurance?” as she chides Fred and smiles.

“Whoops, pardon my gender bias, Jane,” Fred admits sheepishly. “You’re right.” He moves on quickly. “Key *person* policies,” he emphasizes, “should be purchased by Baker Pumps on Jim, you, Bob, and on Sam McCall too.”

“Whoa, that sounds like a lot of money going out,” Bob exclaims.

“Actually,” Fred assures him, “it’s to *prevent* a lot of money going out at some unpredictable time in the future. Let me explain. This is insurance on the lives of valued and skilled employees to partially indemnify the business for the loss sustained upon the death of a key person. During the life of the key person, the life insurance may strengthen the credit of the business and may provide cash for emergency needs. Upon the key person’s death, the life insurance may reinforce the capital structure of the business, may pay for the cost of training a replacement and may solidify lines of credit. The death proceeds are free from income tax. Baker Pump’s credit rating and lines of credit may be adversely impacted by the death or disability of Bob, Jim, or Sam. These ratings and lines of credit can actually be enhanced by the purchase of key person life insurance.”

“That’s something I’ve never even considered,” Bob reflects.

“The purpose of insurance,” Fred confirms, “is to cover risk. The transition of Baker Pumps is one such risk. While you may want to think this option over, Bob, let me add some more ideas for you to think about.”

“With Jim as the successor to the business, it would be wise for him to have full coverage not only of life insurance but disability insurance as well.”

“I don’t understand that,” Bob quickly responds. “Jim is young and healthy. Why should he bear the cost of disability insurance?”

“That’s just the point, Bob,” Fred explains. “The time to get insurance is when you *are*



young and healthy and while you qualify for preferred rates.”

“Preferred rates? What does that mean,” Jane asks curiously.

“There is not a single rate for insurance,” Fred begins. “There is a schedule of cost for insurance depending on the risk an insurance company has to bear to cover a life. Healthier and younger people have less risk. Thus they can get preferred insurance rates. The opposite is true for older people and those who begin to have chronic health problems as they age.”

“That makes sense,” Jane says, following along. “I never thought of that angle,” Joe adds.

“To underline my point,” Fred continues, “should something happen to Jim as a young business executive, the whole question is raised anew of who would run the company and how it would weather disability as well as death. Insurance coverage would provide funds that can be used to help Baker Pumps weather those storms. I believe this is a wise cost to take on. It works the same as key person life insurance, except it pays the company if the key person becomes disabled. The benefit is paid for a maximum of eighteen months. The coverage affords the company time to determine the length of the disability and whether or not someone else needs to be hired on a temporary or permanent basis. I’m not pushing, insurance, Bob, but it is something more for you to consider since you like to have all bases covered.”

“The last thing I have to say about insurance,” Fred says, “is that you have identified a significant role for Sam McCall to play in your business-succession plan. He will be critical to the continuation of the Baker Pump legacy. Without Sam, Jim could well have a difficult time. Sam also fits the description of a key person. In my opinion, action needs to be taken to encourage Sam not just to take on a new role but to continue with Jim as long as you need him.”

“Why wouldn’t he?” Bob asks casually.

“There could be a number of reasons,” Fred reflects. “He may have discomfort in playing a new role in the company. He will have a new status, perhaps become distant from his old buddies who could become jealous. Or, and I don’t know Sam, but he could believe that in his new-found position with the company suddenly believe he is all too valuable, and seek employment elsewhere with visions of better pay and benefits dancing in his head.”

“I find that difficult to believe about Sam,” Jim observes.

“You may well be right,” Fred responds, “but you are dealing with change, and it is difficult to predict how people will respond to change, right Bill?” Fred asks his colleague.

But before Bill can answer, Bob chimes in. “Are you kidding. What we’re thinking for Sam would be an improvement, a good change, not a bad one.”

Bill Smith responds. “It seems to you to be a good change, Bob, but you don’t know what goes on inside Sam’s head. Change—good or bad—is stressful to the individual. Everyone handles it differently. Some fear any change. Others always look for opportunity in change. Either way, change at first is a stress that requires capability to handle.”

“I never thought about good changes as stressful,” Bob murmurs.

“Our brains first register changes as a difference from what we are accustomed to. This registers as a structure-loss, a sense of anxiety. Look at your own response to the idea of foreign markets. What Jim thought of as an opportunity, you thought of as a danger. The same could be true of Sam in his new role,” Bill explains.

“I never thought of it that way, either, Dad,” Jim observes.

“To offset the anxiety Sam might be feeling,” Fred says, picking up on Bill’s explanation, “a benefits package can be created to make the new position even more desirable than the status and pay he would get. A management-compensation package should be developed for Sam as an incentive for him to remain at Baker Pumps. This would include life and disability insurance that I’ve mentioned and perhaps a bonus or deferred-compensation plan as well,” Fred concludes. “Bob, you and Jim should set up a meeting with your insurance agent about these possibilities. He can cost them out for you so you can decide the cost/benefit ratio of each choice. That way, you can make a careful decision based on solid information.”

“You know me too well, Fred,” Bob says gratefully.

“This is not just what I know how you personally would like to proceed, Bob,” Fred responds, “it’s how many successful business people I advise proceed. Consider each step carefully, comparing the benefits of a proposed course of action against the costs. It’s just good business.”

“We’ve covered a lot of estate planning information this afternoon,” Fred says winding down. “We have a few more things on our plate concerning Bob and Sue’s estate. But unless there are any questions, let’s call it quits for today. We can reconvene tomorrow and finish up our agenda then.”

The Baker family members stand up and stretch, knowing they have been through a valuable lesson on estate planning. As long as it has seemed, Fred and Bill have kept the purpose of the retreat in the front of everyone’s minds. At dinner and afterward there will be much informal discussion based on today’s agenda. Nevertheless, the Bakers adjourn, looking forward to dinner together and an evening of relaxation.

## **Reflections**

1. There has never been any doubt in Bob’s mind as to preserving the family legacy to the next and succeeding generations. However, for many business men and women, this possibility is limited because there is no one in the family with the capabilities or the desire to take over the family business. For these individuals, the business will either be sold during their lifetimes or at their deaths either to employees or to outside third parties. In his situation, Bob is fortunate to have his younger son working in the business, who is seen as a result of the retreat as a suitable candidate to succeed him.

2. There are several methods of transferring a business. They include gradual gifting, outright sale of the business to third parties or employees, outright sale of the business to family members, or transfer of ownership by will or trust at death.

3. For some business owners with children active in the business, there are insufficient other assets to give to the inactive children. In such cases, it may be necessary for the business owner to recapitalize the corporation into voting and nonvoting shares. The children active in the business will receive voting shares while those children not active in the business will receive nonvoting shares. Through a program of puts (rights to sell) and calls (rights to buy), the children active in the business will eventually end up owning 100% of the corporate stock, and the children inactive in the business will receive equivalent value when their nonvoting shares are redeemed by the corporation.

4. Regarding a Protective Trust, directions may be given to its trustee as to when to withhold distributions from the trust, such as when there is a pending divorce or lawsuit. Perhaps one of the best protective devices is to give the trustee the discretion to distribute principal and interest among several different beneficiaries (i.e., children and grandchildren), which will make it extremely difficult for a creditor to compel distribution when such projections are in place. A well-drawn trust that addresses situations like Jane's marriage will include a spendthrift clause. This clause will prevent the beneficiary from transferring or conveying his or her rights under the trust and will further prevent the involuntary transfer of such trust assets to spouses or creditors. Most states permit spendthrift clauses.

5. Jane's marriage is a sensitive issue that—as Bob and Sue worried—ends up being referenced in the family forum. But note that Bill Smith makes certain that Jane and Jeff's relationship does not become open to family discussion. Bill makes a point of talking about a variety of uses of a protective trust so that Jeff can see that it is aimed to protect Baker assets rather than to punish him. These are fine distinctions, and very important ones that will have long range benefit to the participants. If Jeff or Jane are potentially embarrassed about the state of their relationship, the retreat is not an occasion to put them in the spotlight. Rather their relationship is treated respectfully and only in the context of the discussion on the future and what must be taken into account to develop a solid multi-generational estate plan.

6. Fred has requested that Bob's financial planner, Susan Jones, do a financial analysis of the effect of the gift-giving program on the Baker's future income needs. Susan's study projects that the gifts will not adversely affect the Bakers' income needs both currently and in the future. The financial planner is an integral part of the estate- planning process, especially in terms of making certain possible gifts will not adversely affect the clients' income needs. As indicated earlier, the Bakers do not live extravagantly, nor do they intend to escalate their lifestyle significantly. They may start to travel more than in the past; but according to Susan, given Bob and Sue's current financial and projected cash needs after factoring in their life expectancies, the effects of inflation, the assumed returns on their investments, and the number of years until retirement, the gifting process will have no foreseeable adverse effect on their income needs.

7. Bob desires to work in the business until age 67. Given his current financial situation, he is not financially dependent now or in the future on his business earnings. Other business owners who have reinvested significantly in their own business, do not have sufficient other assets to live as comfortably as Bob. Therefore, gifting must be considered in light of this dependence on business income. Many business owners need to be encouraged to diversify their assets so they are not as dependent on the business for income. Because Bob and Sue are not dependent in this way, disability insurance through the business is not critical to them, nor are many of the benefits that other business owners seek such as nonqualified retirement and deferred- compensation arrangements.

8. Under the Internal Revenue Code, each person is entitled to give \$13,000 each year to each person they choose, without incurring any gift taxes or filing a Form 709 Gift Tax Return, and without using up any of their \$5.0 million lifetime exemption. This can be a very useful technique for shifting value from an older-generation taxpayer who is concerned about the estate taxes that will be incurred at his or her death to a younger-generation taxpayer.

9. Use of a grantor retained annuity trust (GRAT) is another helpful tool for value shifting. A GRAT would pay Bob and Sue a guaranteed return for a number of years. If the trust investments outperform the guaranteed annuity return, there will be assets left over at the end of the GRAT's term. Because Bob and Sue's financial planner has recommended excellent investments with good returns, Fred informally suggested a GRAT as a value-shifting technique. Bob and Sue decided to postpone the idea for future consideration, however, in light of all the other decisions they had to make. For other clients, this is a very effective estate-planning tool.

10. While Bob and Sue have chosen to begin gifting shares of stock to Jim and his children, many business owners who are dependent on the income from the business are unable to gift and must make transfers in the form of sales. Often these are leveraged sales which take the form of sales in exchange for installment notes, self-canceling installment notes, or private annuities. The sales will freeze the value of the corporate stock but still permit the seller to continue to receive income.

With reference to an installment sale, the purchaser obtains a basis in the amount of the purchase price, and the seller will incur capital gains tax on the sale. The seller will be able to report the gain on an installment basis. If the installment note has not been paid in full prior to the seller's death, then the fair market value of the note will be included in the estate of the seller.

However, in the case of a self-canceling note, the buyer's obligation to pay ceases upon the seller's death, and therefore, such a note can be very beneficial to remove assets from the estate.

In both the installment sale and the self-canceling installment note, there has been a freeze on the transfer-tax value of the asset sold as well as a limitation on the income generated by that asset. Another benefit of this type of sale is that the seller can forgive all or part of the payments due and turn the note into an installment gift. In the event that the seller dies prematurely, there is a significant advantage in using a self-canceling installment note. In reference to the self-

canceling installment note, it must contain a premium for the self-canceling feature, however.

Finally, some sellers who sell to family members take back a private annuity, which again causes there to be no value remaining in the seller's estate at death. If the seller dies, prematurely, there to be no value remaining in the seller's estate at death. If the seller dies prematurely, then the buyer has benefitted, whereas if the seller outlives his expectancy, then the transaction has been more detrimental to the buyer. The annuity payments of course are included in the seller's estate if the money is not spent and provides the seller with a lifetime source of income that is different from the installment obligations which provide income only for the term selected. One disadvantage of a private annuity is that the annuity obligation must be unsecured. And, the seller runs the risk that the buyer will be unable to make payments in the future. Also, the buyer's payments are not deductible as interest.

11. One possibility to help Jim cover estate taxes upon the second to die of his parents is to have the corporation redeem some of the stock, under Code Section 303, from the estate of the last surviving spouse. The corporation could do so using accumulated earnings, but the maximum amount that can be redeemed is the sum of the death taxes imposed and the amount of funeral and administration expenses. Here again, the value of the stock in the gross estate must exceed 35% of the adjusted gross estate. Section 303 allows cash to come from the corporation to the decedent's estate in redemption of the stock. Such a cash distribution is not considered to be a dividend but qualifies as a sale and therefore is treated as capital gains. However, because of the step up in basis of the decedent's stock at the date of death, there should be no gain recognized by the estate and thus no capital gains tax.

12. There is a variety of incentives for maintaining employee loyalty and motivation. In addition to life and disability insurance, they include executive bonuses, non-qualified supplemental benefit plans, deferred-compensation and, split-dollar life insurance.

## Chapter 6

# MAKING ROOM FOR EVERYONE: The Interplay of Family and Community Values

The next morning Fred Smith calls the Baker Succession Retreat back to order for its final session. “We have one more portion to go, everyone,” Fred begins, “and that’s some more discussion about trusts, charitable giving, and the uses of an I.R.A., an individual retirement account.”

### Preserving Assets through Trusts

“When professionals begin talking about trusts, the effect can be mesmerizing. By mesmerizing I mean that our remarks either intrigue our audience with what wonderful estate-planning tools trusts can be, or we put them to sleep. I hope the latter is not the case with us today. Trusts have long names with shorthand abbreviations, sometimes making it hard to follow the idea of what they can accomplish. So just raise your hand if I start losing you.”

“To begin with, let’s suppose that each of you is going on a three-year around the world cruise and must leave behind all your children and possessions. Consequently, you are also required to leave behind a set of instructions as to how to raise your family, run your household, and how to handle any unforeseen events that may occur.”

“That’s impossible,” Jill protests. “How could anyone ever do that. No one could raise my children the way I’d want them to, no one!”

“And how can you predict or forecast unforeseeable or future events?” exclaims Jennifer. That’s impossible too.”

“And our household is so busy,” Jane replies, “I can’t imagine writing down instructions about how to keep it going on a daily basis.”

“And continually changing, too,” Jeff adds. “We’re always planning something new—an addition to the house, plans for the baby, different schools for the kids.”

Surprised at the response his example has elicited, Fred responds spontaneously. “This is great!” he exclaims. “You get my point exactly. These are difficult and complex considerations. But now imagine that instead of planning a three-year vacation, you are planning for your family’s future after you die. How is this different?” Everyone sits in silence as they realize the

significance of what Fred is saying. “You certainly want your values to continue with your children, right? And you want the special things about your family to continue after you’re gone: traditions like gathering at this beautiful retreat setting, a heritage like the community reputation enjoyed by the Baker family business, and values and principles that your family has always stood for—honesty and integrity, caring for one another in good times and bad, and a commitment perhaps to be the best people you can be, personally and professionally. At least that’s how I as an outside observer of your family in the community would view the Bakers.”

“I think you’ve got us pegged pretty well,” Bob says. “I do too,” Sue adds. “These are important values Bob and I have always tried to ingrain in our children.” “And we hope we’re doing the same, Mom,” Jane says, to murmurs of agreement from her siblings and their spouses. “Then that’s the Baker legacy across the generations,” Fred concludes. “And the purpose of trusts is to help preserve and continue that legacy.” “You’ve got our attention,” Bob says. Everyone leans forward in their seats to learn more.

“Part of preserving values and traditions is preserving assets the family has acquired over the years, and then deciding how to best distribute these assets in line with those values,” Fred explains. “For Bob and Sue, I recommend separate revocable trusts that upon death would separate into what are called credit shelter and QTIP trusts. Let me explain what these involve. Under the tax law in effect for the years 2011 and 2012, up to \$10.0 million of assets are protected from estate tax if both spouses were to die in 2011 or 2012. Under the new law of portability, if some or all of the \$5.0 million exemption of the first spouse to die is unused, then the unused portion of that exemption is transferred to the surviving spouse”.

Fred recommends that Bob and Sue not rely upon the portability provisions but, rather, create separate revocable trusts that will provide that, on the death of the first spouse, \$5.0 million of assets will be used to fund the Credit Shelter Trust, and the balance of the assets will fund a Marital QTIP Trust, which will qualify for the marital deduction. After the death of the first spouse, appreciation on the Credit Shelter Trust grows estate tax free until the death of the second spouse.

The marital deduction allows whatever one spouse leaves to the other to go to the surviving spouse free of estate taxes regardless of the size of the transfer,” Fred explains. “There are different ways of getting a marital deduction, including giving the property outright to the spouse, or by giving property to trusts that qualify under the law for the marital deduction. A commonly used marital deduction trust is a QTIP trust, which provides all income to the surviving spouse, power of invasion of principal for the spouse under certain standards (health, education, maintenance, and support) depending upon who the trustee is, and certain other technical requirements. QTIP is short for a lengthy phrase, ‘Qualified Terminal Interest Property.’ The term sounds complicated, but it represents a very important tool in estate planning. I recommend QTIPs be used in this estate plan because they will provide continuing protection for the surviving spouse in terms of asset investing and for protection of the surviving spouse as the years go by.”

Fred goes on. “The marital deduction is unlimited, but in a larger estate we want to make sure that we do not over qualify the marital deduction. By this I mean that we want at least \$5.0 million to pass into a credit shelter trust to properly shelter the first \$5.0 million plus appreciation on the \$5.0 million from estate taxes when the second spouse dies.”

“I like that idea,” Bob concurs, and Sue nods in agreement. “But is that legal?” Bob asks as he absorbs these details.

“It certainly is,” Fred affirms. “Everything I am suggesting to you is perfectly legal and designed to minimize the tax bite from your estate. There’s nothing preventing you from organizing your estate to pay the least taxes required,” Fred explains.

“I’ve heard about zero-tax estates,” Bob continues. “So how does that work?”

“Those estate plans are designed with one primary objective,” Fred explains, “to pay no estate taxes to the Government. But you and Sue, as you’ve told me, have many other priorities— the continuity of the business, taking care of your children and grandchildren, and perhaps making some plans in your estate to support community organizations whose values you share,” Fred offers.

“Yes, that’s true,” Bob concurs. “In line with that,” Fred continues, “if the complete elimination of estate taxes is not feasible, perhaps your next priority would be the minimization of estate taxes. You can accomplish your family objectives while minimizing taxes. But if your goal is to eliminate taxes, then your family objectives must take a lower priority,” Fred explains.

“Oh, no, family comes first!” Bob affirms. “Then your estate can be designed to make that priority first and still take advantage of various, very effective measures,” Fred assures him.

“But isn’t that ‘tax-avoidance,’” Joe wonders.

“Yes, it is,” Fred confirms. “The Government can’t make you pay more taxes than you owe,” he says. “Tax avoidance is fine. Tax evasion is illegal. So-called ‘tax-avoidance’ is perfectly OK as long as legal mechanisms are used. Trusts are among those mechanisms,” Fred explains. “There’s nothing at all wrong with paying the least tax under the law. It’s a smart way to conduct business.”

Fred turns to the flip chart at the front of the room, “”Let me go into the advantages of the credit shelter trust. With an introductory note of caution, “some of these words have technical meanings that we can discuss in subsequent conferences once Bob and Sue agree on an overall plan,” he writes the following:

### ***The Credit Shelter Trust***

1. The trust can have beneficiaries including not only the surviving spouse but the children and possibly the grandchildren as well.
2. If the credit shelter trust appreciates prior to the death of the second spouse, all the



appreciation passes tax-free to the children too.

3. The surviving spouse can have a limited power of appointment to appoint the trust among a class of persons other than himself or herself, his or her estate, or his or her creditors.

4. The surviving spouse can have the power to invade principal for himself or herself based on an “ascertainable standard of health, education, support, and maintenance.”

5. The surviving spouse can be named as sole trustee of the trust provided that the power to invade is under the “ascertainable standard” and that the trust is otherwise properly drawn.

“By properly using the unified credit of the first spouse to die,” Fred continues, “the estate-tax savings will be substantial.”

“I like the sound of that!” Bob exclaims.

“There are additional benefits, too,” Fred continues. “These trusts would, if fully funded before death, avoid probate, will not be open to the public eye, and can avoid guardianships. Bob and Sue would be co-trustees of each other’s trusts during their lives and upon the death of one of them a corporate trustee would become a co-trustee with the survivor of both the credit shelter trust and the QTIP trust, as I’ll explain shortly. This is where your long-term relationship with the folks at First Trust can pay a handsome personal dividend, Bob, because their trust officers can help you or Sue, whoever is the survivor, to implement the provisions of the trusts you are now setting up.”

“Bob,” Fred continues, “you may desire to be sole trustee if Sue predeceases you. And you can continue the same investment strategy Susan Jones has been implementing for you with such excellent success. I would like to arrange a meeting with Susan to have her explain to your children how important financial planning is in your overall strategy. She has been doing a wonderful job investing for many years for you, and you can clearly see the results. However, it is important that a good financial investing strategy also be implemented for your children. Jim, Joe, and Jane should all meet with Susan.”

“Let’s now return to the credit shelter trust,” Fred says as he moves on. “There would be no federal estate taxes payable upon the death of the first spouse, and all of Bob’s or Sue’s assets would remain available for the support of the surviving spouse. These trusts would be established in such a fashion as to fully utilize both of the \$5.0 million generation-skipping exemptions that would avoid estate taxes on up to \$10.0 million of assets on the death of the children.

“What does ‘generation skipping’ mean?” Joe asks with his personal situation in mind. “Are we coming back to my question from the last session?”

“Yes, absolutely,” Fred responds. “This is a provision by which the transfer of assets ‘skips’

a generation. In the case of Bob and Sue, in the year 2012 up to \$10.0 million of their assets can pass to their grandchildren without ever being taxed in their parents' estates. Yet the children can receive income during their lives from the \$10.0 million, as well as principal which may be needed for their health, education, support, and maintenance. I'll continue with generation skipping in just a moment."

Fred continues, "I also am recommending durable powers of attorney and living wills for Bob and Sue. The durable powers of attorney would give each of them the ability to handle financial and medical decisions for each other in the event of incapacity. I often recommend that an adult child act under a back up power of attorney and as health care surrogate."

"What would that involve?" Jane asks.

"This means that if either of the parents is unable to function in these capacities for one another, then one of the children would be the back-up. A durable power of attorney would authorize him or her to make decisions and sign documents on their behalf. As health care surrogate he or she would have the authorization to make health-care decisions, including the withholding of life support if that's what the parents agree to ahead of time," Fred explains.

"That's a lot of responsibility," Jane says hesitatingly.

"It is," Fred concurs. "But it is a responsibility taken with full preparation and informed discussion. The parents make clear their wishes in the living will and in discussions with the surrogate, so the responsibility is not to make new decisions on their behalf but to implement their wishes previously decided and agreed upon. It's a responsibility not to be taken lightly," Fred concludes, "but it is better to be prepared for contingencies than to address them unprepared or at a point of crisis."

"How do you and Sue feel about selecting someone to serve in this capacity, Bob?" Fred asks. "You can choose anyone you wish, but you may want to discuss it and make a decision later."

"We see Jane on a regular basis, and she already keeps in touch with us," Sue suggests.

"And Jim is going to have his hands full running the business, I know," Bob offers. "And couldn't she consult with Jim and Joe anyway?" Bob asks.

"And with due respect to the boys, I'd feel most comfortable with Jane," Sue explains.

"I know how close Jane is to you, Mom," Jim offers, "and I don't think it's a slight to Joe or me to want her to serve, do you Joe?"

"Not at all," Joe agrees. "I'm out of town anyway. I think Jane is the natural choice if she's willing to do it."

Everyone turns toward Jane. "Well," she says a bit sheepishly, "as long as it's OK with everyone, I'd be happy to help Mom and Dad in this way."

“I’d like to add,” Bill Smith observes, “that you certainly have the confidence of every member of your family, and that’s a wonderful tribute to you.”

## **Reviewing Goals**

To reflect a moment on what has been accomplished during this session, the basic estate plan Fred has outlined achieves for Bob and Sue many of their goals plus some others that were implicit and which Fred sought out for clarification. The Bakers had indicated that they wanted to minimize estate taxes, and a key point in achieving this goal is when the first spouse dies. The plan set forth by Fred will allow full utilization of each other’s \$5.0 million unified credit, no matter which spouse dies first. As a result of this marital planning, there will be no estate taxes upon the death of the first spouse. Fred explains that it will be necessary to separate many of their assets to fully fund separate revocable trusts and that he will assist them in this process. The plan also accomplishes their goals of minimizing estate taxes by avoiding tax on up to \$10.0 million of assets upon the deaths of their children by utilizing generation-skipping planning.

Fred goes on, “I’m recommending that 50% of the corporate stock in Baker Pumps be placed in Sue’s name alone so that after the gifting has started, neither spouse will have a majority interest in the business. This provides for the possibility of valuation discounts after both of their deaths.

## **Generation-Skipping Planning**

“Bob and Sue, I know you are very proud of your grandchildren,” Fred notes. “Being grandparents, you have special opportunities to plan your estates in such a way as to save estate taxes down the road upon the death of your children. As we discussed earlier, good estate planning involves not just one or two, but three generations. In most cases, grandchildren inherit their wealth upon the death of their parents, directly through their wills or trusts. Typically, grandparents devise their estates to their children who in turn leave their estates to their children. Along the way, the government taxes this transfer of wealth twice. The estate tax is a tax on transfers of assets, so each transfer is taxed. If there is only one transfer, however, of course there is only a single tax.”

“The generation-skipping tax (GST),” Fred explains, “is intended to keep grandparents from shifting ‘too much’ property directly to grandchildren, thus avoiding the transfer tax at the level of children and grandchildren. The tax rate of the GST for 2012 is 35%. The first tax occurs when the grandparents die, and the second tax occurs when the parents die. As an example, let’s assume that the grandparents’ estate is \$10.0 million, and for purposes of illustration, let’s disregard the unified credit that each grandparent could apply to reduce or avoid taxes. Also, let’s assume that the tax rate is 50% and that between the death of the grandparents and the parents none of the principal is consumed by the parents and that they spend only the income. At the death of the grandparents the estate tax on the \$10.0 million is \$5.0 million, which means that

the parents inherit \$5.0 million. At the death of the parents, the estate is taxed again, with \$2.5 million going to the Government. The grandchildren are left with only \$2.5 million of the original \$10.0 million.”

“Boy, that’s quite a take for Uncle Sam,” Bob observes.

“Yes it is, Bob,” Fred agrees. “If, on the other hand, the grandparents were to leave the estate directly to the grandchildren, the estate tax that would otherwise apply at the death of the parents would be avoided, and there would only be one estate tax. What began as \$10.0 million would result in a transfer of \$5.0 million to the grandchildren, a savings of \$2.5 million.”

“That’s a two and a half million dollars right there,” Sue exclaims. “Can we save that too?”

“Think of this for a moment,” Fred cautions. “The grandparents may object to the transfer of \$10.0 million directly to the grandchildren on the basis that their children would not have any of the benefits of the \$10.0 million. However, it is possible for the grandparents to leave the \$10.0 million into what is commonly referred to as a Generation-Skipping Transfer Trust (GST). The children are entitled to all of the income from the GST trust during their lifetimes and would also have the power to invade the trust under an ascertainable standard of health, education, support, and maintenance. Upon the deaths of the children, the remaining principal in trust would pass estate-tax-free to *their* children.”

Fred continues. “Additional flexibility is given to the children in that they can have a right to determine the apportionment of the trust at the death of the grandparents among the grandchildren as well as spouses of the grandchildren and children of the grandchildren. This is what is commonly referred to as a limited testamentary power of appointment. If the trust is drawn correctly, the parents can serve as trustees of this Generation-Skipping Trust—and there is still tremendous flexibility granted in the use of these trusts.”

“So Jane and I would have a role in the eventual disbursement of these trust funds?” Joe clarifies.

“Yes, you would,” Fred replies, “after Bob and Sue both pass on. This is the advantage of the flexibility I was mentioning. Situations change over the years as do family needs and family relationships.”

“I think we can work together, the three of us, to make the right decisions,” Jane observes.

Bill Smith adds a comment at this point. “The level of cooperation the three of you have shown at the retreat will be a key ingredient in the continuing success of the estate plan’s implementation. If you have any disagreements or differences, simply keep in mind the openness to differences of opinion, the consideration of many options, and a respect for one another—and the decisions you come up with are bound to be in the best interests of everyone.”

“That’s right on the mark, Bill,” Fred affirms. “The formula for success in all of the business and estate arrangements we’ve discussed at the retreat consists of openness, options, and respect

for others. Following that guideline, you will always have flexibility and an eye for new solutions, no matter what may come up.”

In an earlier conversation during a break Joe and Jill had indicated that because they are well-off financially in their own right, they desire that any inheritance that might be received from Bob and Sue be in the form of a generation-skipping trust. They have already done estate planning in their hometown and are well aware of the tax problem that would result from inheriting additional wealth directly from Bob and Sue. Therefore, Joe is wisely suggesting that his inheritance be placed in the form of a GST trust if at all possible. Fred will recommend that Bob and Sue take into consideration Joe and Jennifer’s wishes, so part of the Baker estate plan could be to utilize both Bob’s and Sue’s generation-skipping exemptions to accommodate the wishes of their son and daughter-in-law.

## **Qualified Personal Residence Trust**

Fred then continues his discussion of the estate plan. “We’ve talked earlier about the idea of ‘value shifting,’ Fred notes. There is another value-shifting technique that I believe can be immensely valuable to Bob and Sue. It’s called a qualified personal residence trust, or QPRT for short. The goal is to shift value—from an older-generation taxpayer concerned about the estate taxes that will be incurred at his or her death—to a younger-generation taxpayer. It involves an *irrevocable* gift by the older generation donor of his or her primary residence or vacation residence into a trust. The donor retains the right to live in the residence for a chosen term or number of years, and at the end of the term, the residence is owned by the younger-generation taxpayer as the beneficiary of the trust. Or if the donor does not want his or her children to receive the residence outright at the end of the term of the QPRT, he or she could state in the QPRT agreement that at the end of the term, the residence will be held in further trust for the children until the age chosen by the donor, at which time they will receive their interest outright.”

“Doesn’t this get into how to slice up pieces of real estate like the case of the family limited partnership and turning it into shares?” Joe asks.

“An astute question!” Fred responds. “Please hold it a moment as I explain some of the QPRT details. Take the example of a 62-year-old person who can transfer his vacation residence currently worth \$2.0 million into a QPRT and retain the right to live in it for ten years, at which time the donor wants to pass it to his three children and using an AFR Rate of 1.6%.”

“Why does this example sound so familiar?” Bob jokes.

“Well, I do have a point to make here,” Fred says with a smile, “but you all keep getting ahead of me. What’s a so-called legal expert to do?”

“Enjoy the company,” Bill Smith quips, “and take credit for what a good teacher you are,” he adds.

Fred grins sheepishly at the tables having been turned on his serious lecture. “OK,” he says. “But there is a point to be made here.” Laughing, he goes on. “For estate- and gift-tax purposes, the donor is passing an asset worth \$2.0 million to the children but is considered under the Internal Revenue Service rules and actuarial tables to be making a gift to them of only about \$1,378,460. This is because the IRS considers a sixty-two year old’s right to live in the home for ten years to be worth \$621,540, and this amount is deducted from the value of the asset. On April 15th of the year following the transfer, the donor will file a Form 709 Gift Tax Return showing a gift of approximately \$1,378,460 (\$2.0 million minus \$621,540), which can be applied to the donor’s remaining \$5.0 million amount, resulting in no gift tax owed to the IRS.”

“If the residence appreciates at an annual rate of 4% during the ten years, all this appreciation is also removed from the donor’s estate for estate-tax purposes and is passed to the children. Using this example, if the \$2.0 million vacation residence appreciates at the rate of 4% each year, at the end of ten years it is worth approximately \$2,960,489. If the donor survives for the full ten-year term, he or she will have passed an asset worth approximately \$2,960,000 to the children and used up only slightly more than \$1,380,000 of his or her unified credit amount.”

“That’s quite a deal!” Bob exclaims. “I really see how this value shifting idea works. By making a gifting decision now and locking in the principal amount, all future appreciation is transferred to the next generation and hopefully to a lower tax bracket. That is smart.”

“Yes, it is,” Fred replies. “And this is a great example of the value of proper estate planning. If the donor does not survive the term of the trust (in my example the ten years), however, the residence is included in the estate as if he or she had never made the transfer to the QPRT and is subject to estate tax. Therefore, the term of the trust, while not prohibiting an effective gift, must be carefully chosen based upon the donor’s age and health at the time the QPRT is set up. This beautiful Keys property, I suggest, should be placed in Sue’s name. She would then create a qualified personal residence trust that would allow them to utilize the property for the next ten years, and then the property would continue to be owned by the trust for the benefit of all three children.”

“So getting back to my question, this property would *not* get split into shares,” Joe concludes.

“Exactly,” Fred agrees. “You, Jim, and Jane would share in the benefits of the property. After 10 years it would continue to be owned in trust.”

“So this home would stay in the family, then?” Sue inquires.

“Yes, it would,” Fred agrees.

“That would make me very happy,” Sue smiles, “because all of us have had such great family times here. I’d hate to see this beautiful home leave the family.”

“And it’s a special part of nature,” Bob adds. “South Florida is losing parcels like this all too quickly. Jim and I love the fishing here, to be sure, but the shorebirds, the roar of the tide at

night, and even those silly pelicans diving for fish, are parts of nature that have been special to me for a long time.”

“And for us too, Dad,” Jane echoes. “We’ve been coming here for years, and Jim and Jennifer’s kids, and Jeff’s and my kids are taking pleasure in these same things. And maybe we’ll even see more of Joe and Jill and the baby down here. It’s a magical place.”

“This is a real part of the Baker legacy, it sounds like to me,” Bill Smith observes. “You are fortunate to have this beautiful piece of Creation to enjoy and to share with one another. It is special, Jane, and it helps foster family bonds that are hard to create in today’s busy world. I think the idea of preserving this property in the family is right on target.”

Then in conclusion, Fred suggests, “now let’s take a break, and we’ll come back and talk about another opportunity for the Baker legacy—charitable giving.” Everyone stands and stretches, curious about what Fred has in mind.

## **Charitable Giving**

Fred calls the Baker clan back into session. “Bob and Sue, at our first meeting, I mentioned the estate-planning advantages of making a charitable gift. At that time, you were uncertain of what you might do, though we did discuss the Goodall Clinic and your local church. Have you given this any more thought since, then?” Fred asks.

Before they can respond, however, Jim interrupts. “Why would they want to give money away?” he asks. “Can’t the family use an inheritance rather than giving it to some charity?”

“You raise a very good question, Jim,” Fred responds. “On the face of it, there may seem to be scant advantage for your parents to make a charitable gift. But because a significant part of their assets consists of low basis, highly appreciated stock, there are some tax advantages if they include charitable giving in their estate plans.”

“Charitable giving, however,” Fred notes, “is not just a matter of taxes and numbers. Philanthropy comes from the heart. At this point in their lives your parents are in a position to look back on their lives to see what it is they truly value and how they would like to see these values maintained—or even enhanced—for future generations. They understand that community institutions have played a role in helping them achieve their success—in providing an environment for spiritual growth for their family, in providing a high-quality education for you and your siblings, Jim, in advocating the case for the environment in support of the beautiful life you enjoy here in the Keys. Many people at your parents’ stage of life reflect on these issues, are grateful for the life they have, and want to ‘pay back’ something to the community. In terms of the point you raise, most people like your parents want to take care of family first. Often, however, they want to take care of social concerns as well, and they can do that without detriment to their family. Some, by the way, also consider the effect on the next generation of inheriting large sums of money. They want to provide for their children, but at the same time

they don't want to diminish motivation for making it on their own like the parents had to. These are very important factors that go into peoples' decision about making charitable gifts."

"But not to get sidetracked, let's get back to some of the tax advantages of including charitable giving in your parents' estate plan."

"Before you go into those, Fred, I want to make a comment," Bob interjects. "Your comments hit the mark for me. And the experience of this retreat has caused me to do a lot of thinking. I'm a very lucky man. I'm married to a wonderful woman who's been my partner for over forty years, through thick and thin. And this retreat has shown me just how fortunate I am as well to have a wonderful family—of whom I was proud before, but now as a result of the retreat I'm even more proud. It occurred to me that the person who may get the most satisfaction from what we're accomplishing here today is my Dad. Since he had that open-heart surgery four years ago at the Goodall Clinic, he's had a new lease on life. I thought that since Mom had passed away a year earlier, he'd just pack it in. But he's doing great, eating and exercising like I wish I could. And when we talk about where Bob Baker has come since he worked in that grocery store of his father's, well, I think Dad is just as proud as I am now. Part of my coming to the decision about estate planning, passing on the business, and deciding to smell the roses goes back to Dad's heart attack. I'm not invincible either. But the last four years I've had with him has really helped me open my eyes and made me want to live my life without a heart attack. I'm so grateful to Dr. Henderson at the Goodall Clinic that I'd really like to do something for them. Didn't you say that they're doing some new research on heart surgery, Fred?"

"Yes, I did, Bob," Fred recalls. "They're a non-profit organization, and they use contributions to conduct cardiac research and to train physicians in the surgical techniques that saved your Dad's life. They're quite an outfit."

"Well, I want to do something for them, even if it's not tax-advantaged. Jim, there's no price you can put on a human life. And while I understand your question about who should receive the Baker inheritance, I think there's room for a charitable gift here, right Fred?" Bob expounds.

"I admire your feelings for your father, Bob," Fred responds. "And yes, the Goodall Clinic can use contributions to continue the very work that saved his life. But surprisingly, if you choose a charitable remainder trust (CRT), you can 'have your cake and eat it too' as they say. Let me take a moment to explain."

## **The Charitable Remainder Trust**

"Through the use of a charitable remainder trust," Fred continues, "you and Sue can transfer highly appreciated growth securities that are currently paying a low dividend. These securities may be held or sold by the trust which pays no income taxes because it qualifies as a charitable trust. The terms of the trust can provide either an annuity payment or a unitrust payment to you and Sue for the rest of your lives. You select a payout percentage of at least 5%. The annuity trust payout is then fixed at that percentage times the trust principal. The payout will never



change for your lifetimes. The unitrust payout is a fixed percentage times the trust principal, reevaluated at the end of each year. The unitrust payments may then increase or decrease as the value of the trust corpus increases or decreases annually. You and Sue, as the donors, select who will receive the annual payments of income from the trust, and you can name yourselves as the payment beneficiaries, or even another family member such as a child or a grandchild.”

“I think, Bob and Sue, that your wishes may be fulfilled and your goals accomplished,” Fred continues, “by establishing a charitable remainder trust, with yourselves as the income beneficiaries, with the remainder of principal, *i.e.*, what remains of the underlying asset, going to the Goodall Clinic after you both are gone. You and Sue receive for life a payout of 5%. If your planner invests the trust funds as well as she has invested your money, even after a 5% payout and administrative expense, the trust principal should keep growing. You have two choices—the annuity trust and the unitrust. In the annuity trust, your 5% payout is fixed for the life of the trust, so if you donate assets worth \$500,000, you would receive \$25,000 each year for the rest of your lives. But if you choose the unitrust format, which I recommend since you and Sue are relatively young, then the 5% payout is based on the annual value of the trust assets; so if the principal trust grows over the years, your payout would as well.”

Fred goes on to say that the charitable remainder trust requires one or more trustees. The trustee(s) can be any one or more of a number of individuals or organizations. Bob and Sue may choose to serve as trustees, and if that is the case the trust must be carefully drawn so as not to contain certain powers. Furthermore, they should not serve as sole trustees if there will be difficult-to-value assets in the trust. A common practice is to have a trust department serve as co-trustee, Fred points out. “Mike McKinley of First Trust again may be the person you’ll want to speak with, Bob,” Fred suggests, “about this trust as well as the others I’ve recommended. And the more you have managed by them, the lower the overall administrative costs may be as well.”

“Boy, I guess when you said there were a number of members on my estate-planning team, you weren’t kidding,” Bob observes.

“As my mother always said,” Fred admonishes, “if you want to do something, do it right the first time.”

“I’m glad the mothers are getting credit for something in this arrangement,” Sue says with a smile.

“But I should add,” Fred quickly responds, “a counter to another folk saying, and that is in financial matters, ‘if you want to do it right, don’t do it yourself.’ As you can see from our discussions, these are complex matters, all very intertwined. It’s wise of you both, Bob and Sue, to count on your team of financial advisers to maximize the success of your estate and business plans.”

“This all sounds too good to be true,” Sue observes. “We make a charitable gift and get an income for life?”

“Not only that,” Fred says, taking her question one step further, “you and Bob would also

receive an up-front charitable income tax deduction for a portion of your gift.”

“And if what you say is true,” Bob notes, “my 1% to 2% dividend paying stock is converted to a 5% annual payout!”

“Exactly. And not only that, Bob,” Fred continues, “you will pay no capital gains tax on the low-basis stock you use to fund the trust.”

“That’s quite a package!” Bob observes. “And you thought we were going to throw away the family inheritance, Jim,” Bob laughs, teasing Jim. “I guess maybe the younger generation doesn’t have all the answers.”

“Not yet,” Jim teases back.

Fred also mentions that there is another way to fund a charitable remainder trust, with corporate stock in Baker Pumps instead of the low-basis stock Bob and Sue had accumulated over the years. He wants to review this option with them before they make their final decision regarding the charitable remainder unitrust. “The way this could work for you,” Fred begins, “is that your contribution is made to the trust not in publicly traded stock but instead in corporate stock in Baker Pumps, Inc. The corporation may sometime in the future redeem the stock from the CRT, and, of course, the trust is not subject to capital gains tax on the stock redemption. The cash proceeds from Baker Pumps, Inc., would be reinvested by the CRT to pay the unitrust payment to Bob and Sue for the rest of their lives. If Baker Pumps, Inc., has accumulated earnings, this is one method of reducing those accumulated earnings avoiding a double tax on the money.”

At this point, Jim speaks up. “I know Dad is the one who hates to be taxed, but when I hear Baker Pumps and double taxation in the same sentence, it gets my attention now. And after what you said, Dad, I was thinking that maybe a donation to the University of the Southeast might be a good idea. Certainly the university is part of the Baker legacy since so many of us have gone there, and it might be a way for Baker Pumps and their business school to have more in common. What do you think?”

Bob responds, “Now let me get this straight. Two minutes ago you were concerned about giving your inheritance to a charity, and now you want me to increase our charitable contributions? A gift to Southeast may be something *you’ll* want to consider down the line. You could contribute the corporate stock you’ll be inheriting, for instance; and it may be a very good business move for you. Right now I’m partial to the Goodall Clinic.”

“Let me complete the explanation of the use of corporate stock in the CRT before you make a final decision, Bob,” Fred suggests. “You should know that in order to avoid capital gains tax on funding the charitable remainder trust, there must not be any binding obligation on the part of the trust to sell the stock contributed, because this may result in the IRS arguing that there has been a ‘step transaction.’ What happens in a step transaction is that the IRS treats several actions as one taxable transaction, and therefore it is important to prove that each step in the transaction has independent significance and that the charitable remainder trust has no legal obligation to

allow Baker Pumps to redeem the shares. The IRS has announced in a Revenue Ruling that they will not challenge these types of transactions unless the charity is legally bound or can be compelled by the corporation to surrender the shares of the corporation for redemption. If such a transaction were to be entered into, there must not be any prearranged binding agreements or legally enforceable obligations under the law.”

“That all sounds awfully complicated, Fred,” Bob wonders out loud.

“Not really,” Fred explains. “However, you should know there has been a recent United States Circuit Court decision casting some doubt on the IRS position. On the other side of the issue, however, you should also know that major charities around the country have conducted such transactions successfully and to the satisfaction of their donors.”

## **Charitable Giving and Community Values**

“I like using the low-basis stock approach best,” Bob concludes. “What do you think, Sue?”

“I think that way is best for now, and if Jim wants to do something with corporate stock and a charitable contribution that would be up to him. But I would like to increase our contributions to our church, Bob,” Sue says. “First Church has been like a member of our family since Joe was born. All the children were baptized there, and now Jim and Jill’s, and Jane and Jeff’s kids have been baptized and attend Sunday School there too.”

“Mother,” Jane suggests, “why not use some of the income you’ll be getting from the remainder trust to make annual contributions to the church?”

“Why that’s a wonderful idea, Jane,” Sue responds. “We can increase our contributions to the church that way. I’d really like to do that, Bob.”

“That’s fine with me,” Bob says.

“And you can just make cash contributions as you wish,” Fred notes. “You don’t have to make any special arrangement like a trust.”

“How about a pledge, though?” Jane asks. “Our church has a fund-raising campaign to build a new community and educational center.”

“Oh yes,” Sue exclaims, “I would like to do that.”

“You told me at dinner last night how close you were to your parents, Sue,” Fred adds. “And you might want to make a gift in their memory, perhaps even ask that a plaque be placed with their names on it in the new educational wing.”

“Why, that’s a great idea, Fred,” Sue responds. “Mother was a teacher, and it would be a wonderful way for the entire community to remember her and Dad. They were so active in the community in so many ways.”

“You can make a campaign pledge directly with the church, making annual installments for a number of years, so it’s an easy way to make a gift, and it sounds like a very nice way to carry on a legacy from your side of the family,” Fred observes.

“Yes, I like that. Let’s do it, Bob!” she says enthusiastically.

“Yes, I like the idea too, Sue. It will be a great way to remember your parents.”

The Bakers ultimately decide to use their low-basis stock to fund a \$500,000 charitable remainder unitrust with the Goodall Clinic as the remainder beneficiary. And Bob and Sue also decide to use part of their annual \$25,000 payout from the trust to create a memorial to her parents at First Church as part of their building campaign. The idea of a plaque commemorating her parents is so appealing to Bob, he wants to ask the Goodall Clinic about the same to honor his father and mother. The charitable legacy Sue and Bob are establishing honors their own parents and sets a precedent for the next generation of Bakers to follow if they are so inclined.

## **Planning for IRA Distribution**

As is the case with many business owners and professionals, Bob has a significant IRA account, a rollover from a previous qualified plan that the company terminated. “An IRA,” Fred begins, “is a wonderful asset. It accumulates money tax-free and permits withdrawal at a time in a person’s life when they are supposedly in a lower tax bracket—that is, retirement. Bob’s IRA is the final asset to be considered as part of your estate plan. Deferring receipt of the IRA’s distributions for as long as possible will allow continued investment of the funds that would otherwise have been used to pay income tax.”

Fred further explains that the main benefit of retirement plans is this ability to accumulate money without current taxation. At such time as the money is withdrawn from the plan, there will be taxation on the funds withdrawn at the participant’s current income tax rate. Also, Fred discusses the new minimum distribution rules and the fact that distributions must begin when Fred attains age 70 and 1/2.

“I recommend,” Fred continues, “that Sue be the beneficiary of Bob’s IRA. This would allow her, at Bob’s death, to roll over the balance in the IRA to her own IRA. She could then name the children as beneficiaries. By naming Sue as his beneficiary, Bob would calculate his required minimum withdrawal starting at age 70 and 1/2 based upon their joint life expectancy. This would allow smaller withdrawals and longer tax-free accumulation of the money. Upon Bob’s death Sue would roll over the IRA and be able to set up a withdrawal schedule starting when she reaches age 70 and 1/2, based on her life expectancy and that of her oldest child with a single recalculation. Sue is then permitted to name her children as beneficiaries of the IRA. When Sue passes away, the distributions would then be over the life expectancy of the oldest child at that date. This form of retirement planning allows the spouse to have full access to the IRA money if necessary but also allows her to withdraw money on a very gradual basis and continue the tax-deferred accumulation of money for as long as possible. This form of retirement

planning has been referred to as the ‘eternal IRA.’”

“There is another solution to posing heavy taxes on your IRA, Bob and Sue,” Fred notes. “Based on what Jim said when we were discussing charitable remainder trusts, this may be of interest to you. From time to time each of you has expressed affection for the University of the Southeast, and I know that’s where you first met one another. Jim and Jane have followed in your footsteps there: Jane, like you Sue, met her husband there. This solution involves making the beneficiary of the IRA a charitable remainder unitrust (CRUT). The payment beneficiary of the CRUT at Bob’s death would be Sue. The payment interest for Sue qualifies for the marital deduction and the remainder interest passing to the University of the Southeast at the time of Sue’s death qualifies for the estate-tax charitable deduction. Therefore, at Bob’s death, there should be no estate tax nor should there be any estate tax at Sue’s death. The only income tax paid will be paid as the Unitrust payments are made to Sue; but upon her death, the remaining balance in the trust will pass to the charity income-tax free. Another alternative, of course, is to make the charity an outright beneficiary.”

### **Family versus Charity?**

Listening carefully to Fred’s argument and both options for the IRA, they look at one another. Bob is the first to speak. “I do like the idea of the IRA benefitting the university. And it may have some benefits for Jim’s affiliation with their business school down the road too. But I want to know what you think.”

“My only concern, Bob,” says Sue, “is that the children might be missing out if we took that option.”

“I think they’re going to be taken care of pretty generously already, honey,” says Bob making a point. “And I don’t want our inheritance to minimize their motivations for making successes of themselves on their own terms. There’s a lot of talk these days from people far wealthier than we are about not spoiling their adult children with mega-inheritances. Any thoughts in this area, Bill or Fred?”

“The choice is really yours and Sue’s,” Fred responds. It’s a very personal decision. What do you think, Bill?”

“It is a personal decision, I agree, Fred. My observation is that all the discussion so far has been to protect Baker Pumps and protect the children, or at least provide a platform from which they all can seek their own levels of success. There’s no guarantee of success with money or without it. But it seems to me that the basis of your decision-making has been to help Jim enhance the business and to help all three Baker children enhance their lives and the lives of their children with opportunities they otherwise might not have. I haven’t heard you say you want to make them financially independent, however.”

“I think we should go for the trust for the university,” Sue says, agreeing with Bob. “What’s

your reaction to all this, kids?” she asks.

“Why, it would be a nice way to solidify the relationship with Baker Pumps and the university,” Jim says, “so I’m all for it.”

“Whatever you and Dad decide, Mom, is fine with me” Joe responds. “I think you should follow your hearts. You’ve taken care of the next generations of Bakers quite well, I think.”

“I agree with that plan too,” Jane says. “After all, it’s your money, not ours. What I’ve felt today is that you truly care for Joe and Jim and me and our families. The plans you’ve settled on, having the retreat, and including us in the first place speak volumes of your love for us. I feel very proud to be a Baker and actually kind of privileged to be part of the legacy you’re establishing. Maybe I’m a bit sentimental, but I think what you’re doing is great,” Jane affirms.

“That’s a great note on which to bring our discussions to a close, Jane,” Fred says as he prepares to wrap up. “I believe what your parents are doing is great as well.”

“As do I,” Bill confirms.

Fred continues. “A couple motivated by love of family and caring for their community as you are, Bob and Sue, can create a wonderful plan for the future. This is exactly what you have accomplished these past two days. You have laid the groundwork for passing along Baker Pumps, Inc., to the next generation of Bakers. You have in place a solid blueprint for management succession under Jim’s leadership and Sam’s guidance. Further, you have an agenda to go forward to implement a gradual change of leadership and of ownership that has creatively used the resources of all of your children—not just Jim, but Jane and Joe as well.”

“Building on that foundation,” Fred continues, “you have developed a complete estate plan that supports the future of two generations of Bakers as well as nourishes those community institutions which have nourished you and your family. Your accomplishment is very special, and you are to be congratulated.”

## **Getting Closure: the Bakers Reflect on Their Accomplishments**

“We couldn’t have done it without you and Bill, Fred,” Bob responds.

“I agree,” Sue adds. “Thank you to both of you for your role in making this weekend happen.”

“When I think where Sue and I began that day in your office, Fred, it’s hard to believe we’ve come so far,” Bob says with gratitude. “The business was feeling like a millstone around my neck,” he recalls. “I had no clear idea of what to do, just that I needed to do something!”

“And we weren’t sure about how the kids would fit into our plans either,” Sue continues. “We were full of concern and worries. You both (nodding to Fred and Bill) have helped us find solutions to difficulties that didn’t seem to have solutions.”

“And to find solutions to things we hadn’t thought much about too,” Bob adds, “like estate taxes, what to do with this Keys property, and—really what warms my heart—what we are able to do through charitable giving. I never thought of myself as a philanthropist, but I certainly do now, and it’s a great feeling.”

“Mom and Dad, I’m pleased that you invited us to be part of your planning,” Joe says, following up on his parents’ sentiments. “Jill and I debated about coming down for the retreat, and after experiencing this time with my family, I’m glad we did. I feel connected in a way I haven’t for a long time.” Turning directly to Bob, he continues, “Thanks for being so honest with me, Dad. If anything had happened to you before we cleared the air, I think I would have felt horrible. And to have a chance to be part of Baker Pumps, even in an advisory capacity, lets me have part of a dream I’ve had since I was a boy. It’s a great feeling for me too.”

“What a nice endorsement of your parents’ decision, Joe,” Bill observes. “I’m sure they have some feelings about your participation here too.”

“I certainly do,” Bob says, responding to Bill’s invitation. “I’m glad we’re able to count on you as part of Baker Pumps, Joe. It’s a thrill, actually, to have you aboard. I’m proud to be able to have you to carry on the family business, Jim, and to have you actively involved, Jane,” he says, looking at each of his children in turn. “It’s really a dream come true for me. I hadn’t realized how much it meant to me to have my children as part of my business.”

“Your openness, Bob,” Bill says, “is what has helped make your dreams come true. Putting down Superman’s cape and embracing the role of statesman really enabled you to shift your attitudes toward your family as well as the business.”

“And to our future, together, too, I think,” Sue adds.

“I guess you’re right, Bill,” Bob confirms. “I was ready to make a change, but I wasn’t clear about what to do. I guess I was more ready than I imagined.”

“I’m sure glad we discussed the business,” Jim begins. “I’ve felt up in the air for some time now, and didn’t know how to approach you about it, Dad. The retreat provided the opening. Thanks, Dad and Mom, for coming up with it. I see a lot of things to be decided down the road, but I feel we have a plan to help us.” Pausing a moment, Jim continues. “Actually, it’s not just a plan, it’s a new way of talking that I see as really helpful. Dad, I see you listening to me, and—whether you agree with me or not—I feel we can honestly disagree, but come up with solutions for the challenges in the market Baker Pumps is facing. I can’t tell you the worries I’ve had and how relieved I am that I can talk to you about them—the competition, the employees. I feel we’re on the right track!”

“I do too, Jim,” Bob responds. “It’s great to have confidence in you and your abilities. I think together we can keep Baker Pumps on top—where it belongs.”

“What a great statement of corporate mission,” Bill notes.

“Don’t forget me, too, Dad,” Jane says, making sure her voice is heard.

“Oh, don’t worry, Jane,” Bob assures her, “after taking me on here there’s no way I can forget you. I’m sorry I’ve ignored your contributions to the business. I haven’t meant to, I . . .”

Jane interrupts him, and says, “You don’t need to explain, Dad. What’s important to me is that I have a place at Baker Pumps too, and whether it’s a formal role as office manager—which I think I’d really like—or some other way we work out, I feel you understand that I want to be a part. Actually, I feel you want me to be a part, and that’s important to me.”

“Your openness, Bob, has certainly been returned in spades by your children,” Bill observes. “That must be a good feeling.”

“Good? It’s great!” Bob responds. “I couldn’t be more pleased. Knowing that my company will be in competent and caring hands is the best feeling of all.”

“Then why don’t we return to your ‘Successful Succession List’ to see how things stack up with your business-succession agenda, since that’s where we began our retreat.” Turning to the flip chart one final time, Fred reads the list aloud.

***“Bob’s Successful Successor List***

1. ***Takes*** charge
2. ***Cares***, has a sense of ownership
3. ***Good*** technical manager
4. ***Tough*** manager
5. ***Has*** market savvy
6. ***Understands*** operations and sales.”

“It occurs to me, Bob,” Fred reflects, “that this isn’t just a list of managerial qualities for Jim, but it’s a list as well of business functions required for Baker Pumps to endure and thrive. What do you think?”

“I think you’re right, Fred,” Bob agrees. “We’ve addressed each of those functions these past two days. Between the plans we’re putting in place, and the involvement of Jim, Joe, and Jane, the business is getting taken care of. Look,” he reflects, “Jim will be taking charge of the business in a way I feel comfortable with, and clearly he, Joe, and Jane will have very caring input as well. With Sam’s guidance, and my supervision, I believe Jim can have the managerial savvy by the time I retire to have a solid handle on the business. And I expect you to ask my advice even after I retire, Jim, just so you know.” “Absolutely, Dad,” Jim responds. “I’m



counting on that for the business and for my peace of mind.” “And with Jane and Joe involved in some of the operational details, I think Baker Pumps will have an excellent chance to make it to the next generation,” Bob concludes, “. . . and maybe even to the third generation,” he says, nodding to Jim with a twinkle in his eye.

“I like hearing you talk about retirement, honey,” Sue says. “I want you around for a long time so we can enjoy our lives together. These past 40 years have been great, and I want our next decades to be devoted to us,” she says with a warm smile. Bob returns her smile, and says, “What more could a guy want!”

The retreat concludes with various plans being made and sundry good-byes. Fred and Bill slip away, knowing that they have helped the Bakers create a foundation for their future. Having set a business-succession and estate plan in place, they know, will help preserve the values, the relationships, and the business interests the Bakers hold dear. The Baker legacy will be not only preserved, but hopefully enhanced for the next generations. This is the promise the Bakers have set in motion for themselves.

## **Reflections**

1. Revocable trusts are very effective devices to avoid probate, to avoid costly and time-consuming guardianships, and to provide a mechanism for clients to separate assets so as to fully fund the \$5.0 million credit shelter trust of the first spouse to die.

There are very few drawbacks to doing revocable trusts. They are relatively simple and inexpensive to establish. Clients should not assume that revocable trusts are overly complex. Wealthy clients can easily save substantial sums by properly utilizing both spouse’s Unified Credits. If the parents’ children are wealthy in their own right, strong consideration should be given to generation-skipping trusts to avoid additional transfer taxation on the parents’ assets in their children’s estates when the children pass away.

2. Clients need to realize that tremendous flexibility can be given to the surviving spouse to deal with the Credit Shelter Trust amount.

3. The appreciation on the \$5.0 amount in the credit shelter trust also escapes the estate tax.

4. The clients should have durable powers of attorney, healthcare surrogates, and living wills to express their wishes concerning life support in the event of terminal illness.

The selection of Jane as backup to hold durable power of attorney and as a health-care surrogate is based on her devotion and loyalty to her parents. Though her marriage may be unstable and her judgment about staying with a seemingly undependable husband has been criticized, her qualities of loyalty and devotion are now seen as strengths rather than liabilities.

5. Qualified personal residence trusts are an effective device to permit parents to reside in their residence or vacation home for several years while simultaneously beginning to shift the

appreciation immediately to their children. Because the interest of the children will take effect many years in the future, the tax cost in making the gift is small in comparison to the overall value of the property and is thus an effective value-shifting technique.

Establishing a qualified personal residence trust (QPRT) is an excellent way to shift value to the next generation at a small transfer-tax cost. The biggest disadvantages of the QPRT are the loss of a step-up basis to the children and the fact that the parents will need to rent the property back from the children after their term of occupancy expires.

6. The QPRT is not well-suited either for passing the residence to grandchildren, due to the generation-skipping tax rules or for transferring a residence with a mortgage against it. During the term of the QPRT the donor has the exclusive use of the residence. If the donor wants to continue to use the residence after the end of the term, he or she must rent it from the donees and pay a fair market rental value. Also, for income tax purposes, during the term of the QPRT, the donor is taxed as the owner of the residence on all of the trust's income or capital gains. Therefore the donor may want to transfer a personal residence that does not generate any significant amount of income. Also, the donees take the donor's basis on the residence and do not receive a step up in the basis of the value of the home at the donor's death, which would otherwise be the result if the donor owned the residence at his or her death. Under IRS regulations, the grantor is prohibited from buying back the residence during the term of the trust.

7. Parents whose children are wealthy in their own right should consider using generation-skipping trusts to avoid tax on the assets when their children die. Each individual has a \$5.0 million generation-skipping exemption (see Appendix D).

8. Financial planning is an extremely important part of the Bakers' overall plan. Bob's financial planner has been doing an excellent job of investing for many years, and Fred wants to make certain that all of the Bakers' children understand financial planning and the impact it can have on the overall plan. In addition the Baker legacy will not be passed along to the next generation if there are not sufficient funds at each step of the way. Since Bob has been busy making Baker Pumps a success, he has not had time to educate his children himself about the essentials of financial planning and money management. The transfer of the business is an excellent occasion to have his children educated financially, since he has their attention and motivation at this critical juncture in the family business.

9. Individuals who have accumulated substantial assets over a lifetime have frequently developed contacts with charities. They will no doubt have been approached by charitable organizations for substantial gifts, and in many instances the clients are very inclined to make a gift but do not know how to do so. They will appreciate being educated on the tremendous tax benefits available in making charitable gifts. The professional's efforts may well facilitate a substantial gift. There is nothing more satisfying professionally and personally than assisting a client in completing a large charitable gift.

10. All individuals receiving an income interest from a charitable remainder trust must be living when the trust is created, so, for instance, unborn grandchildren could not be named as

income recipients. This is because the life expectancy tables the IRS uses to determine the charitable deduction for the trust presumes a fixed number and predictable life expectancy of the beneficiaries concerned. The donor(s) can also name more than one beneficiary if so desired. If the unitrust option is chosen, then the principal must be revalued each year, and the subsequent year's payout is based upon that revaluation. Also, a difference between the annuity trust and the unitrust is that unlike the unitrust no subsequent contributions can be made to an annuity trust after the first contribution is made.

11. The donors receive an income tax deduction in the year they establish the CRT. They also have available a five-year carry forward of any deductions not used in that first year. There are certain restrictions based on the donor's adjusted gross income as to how much may be deducted in any one year. Because the contribution consists of appreciated property, the charitable deduction is limited to 30% of the Bakers' adjusted gross income.

Also it should be noted that when an individual establishes a charitable remainder trust, the income tax deduction is calculated on the value of the remainder interest given to charity at the death of the last income beneficiary. The IRS has tables to calculate the charitable deduction. There are also numerous computer programs that will compute the deduction.

12. A unitrust is generally preferred by most younger donors because of the hedge against inflation. However, the annual payout can decrease if the value of the trust decreases. Older donors may prefer the safety of a fixed annual return and thus prefer the annuity trust; or they may find the simpler charitable gift annuity more to their liking. The latter does not involve the complexity of a charitable trust but has many of the same advantages in its fixed return and charitable deduction.

13. There are three types of charitable remainder unitrusts (CRUTs). The standard CRUT provides that the trust assets, multiplied by the payout rate, must be distributed to the beneficiary. If the investment return exceeds the payout rate, the beneficiary will enjoy an increasing income. The beneficiary receives the stated payout rate multiplied annually by the fair market value of the trust assets, even if the trust's actual income is less than the calculated payout. Standard CRUTs fit well for older clients who must rely on trust payments during retirement.

The second type of CRUT is a net income unitrust which will pay the beneficiary the lesser of the payout rate or actual trust income but does not provide any means to make up payments in which ordinary income is less than the payout rate. For this reason, the net income trust is very rarely used.

The net income with makeup CRUT requires that the beneficiary receives the lesser of the payout rate or the actual trust income; but if the trust income is less than the payout rate, then in subsequent years when trust income is greater than the payout rate, all of this income must be paid out up to the total of the current year's payout rate, plus any deficiencies from prior years.

14. The remainder of the CRUT goes to a charitable beneficiary after the death of the last income beneficiary. The remainder interest may be distributed to one charity or may be divided

among several charities. The selection of the charities is made by the donor, who may retain the right to change the charitable beneficiary during his or her life or at death by will.

15. Many clients feel a strong sense of gratitude to charitable organizations and feel a desire to give back to their community some of the wealth that they have accumulated. There are many tax and nontax incentives to making lifetime gifts as the Baker case demonstrates. Among these are the trust's ability to sell low-basis, highly appreciated stocks with no income tax; the client's ability to retain for life a significantly higher income from the assets than was previously available; the avoidance of all estate taxes on the assets transferred into a charitable trust; the receipt of a significant income tax deduction in the year of the gifting to the trust and up to five more years to carry forward any unused portion of the deduction; and finally, the satisfaction of knowing that after the donor's death, the charity will be using the donor's assets to carry out a charitable mission to the future generations of those it serves, whether in health-care, religion, education, the environment, the arts, or another social mission.

16. Given the increased yield from the trust's tax-free payment portion, capital gains, and subsequent reinvestment, there will be annual cash flow to the Bakers beyond what they could have achieved with their own sales and after-tax investments. They may use these funds to help pay premiums on the life insurance policies mentioned earlier or to make the \$11,000 annual gifts to their children. As we saw earlier, Bob and Sue decide to use these funds to make gifts to an additional charity, First Church.

17. Assume the Bakers take \$1.0 million of publicly traded stock with a cost basis of \$50,000 that generates only 2% yield annually. If the Bakers are in the 15% capital gains bracket and sell the stock, they will pay a capital gains tax of \$142,500 ( $15\% \times \$950,000$ ), leaving them \$857,500 to invest for retirement. If they gift the \$1.0 million through a CRT retaining a 5% payout annually and allow the trustee to sell the stock and reinvest the proceeds in income-producing assets, the net result is that retirement income over their lifetimes will increase, since they will have the entire \$1.0 million working for them, not just the \$857,500.

18. In selecting a payout rate for the unitrust, paradoxically it *may* be more beneficial to the income recipients to select a lower payout rate than a higher one. This is because over the life expectancy of the beneficiaries, if a payout rate - say a high rate of 10% in a standard CRT - is selected, it may cause the principal of the trust to diminish each year. The net result is that the beneficiaries will have 10% of a diminishing amount, not a constant amount or an increasing amount. Computer projections can help in selecting the most beneficial rate over the projected lifetimes of the beneficiaries. Some established charities may provide assistance with these calculations.

19. If a CRT is established using corporate stock from Baker Pumps to fund it, it should be noted that the CRT cannot own 80% or more of the stock of the corporation because the corporation is then considered a controlled corporation, and interest, annuities, royalties, and rents are considered unrelated business taxable income, with a resultant loss of the charitable remainder trust tax exemption for the year.

20. Because of the large impact of taxes on IRAs, they are excellent assets with which to make a charity the beneficiary.

21. For the client who desires to retain the IRA in his or her family for as long as possible, the spouse should be named as beneficiary. Upon the death of the first spouse, the surviving spouse will roll over the IRA, name the children as beneficiaries, and continue the tax deferral for as long as possible. This form of retirement planning is commonly referred to as the “eternal IRA.”

22. An IRA is an excellent method of planning for retirement, but it is not a good device to pass wealth to family members at death. At death there is the possibility of at least two separate taxes coming into play. The first tax is the estate tax, which for estates in excess of \$5.0 million is 35%. Next, the proceeds of IRAs paid after death are “income in respect of a decedent,” taxed as ordinary income to the beneficiary. Consequently, the beneficiary receiving the money may be subject to income tax up to 35% which is the maximum rate for 2012 (although the beneficiary may receive an income tax itemized deduction on his or her income tax return for federal estate taxes attributable to the IRA). This may lessen somewhat the double tax on the estate tax paid.

23. The advisor’s role in planning for IRA distributions is a difficult one. The advisor must advise the client of the proper beneficiary designations and correct required minimum distribution requirements beginning at age 70½. The advisor must also properly advise the client of the benefits of the tax-deferred accumulation and warn the client of the double tax. Because of the latter, a charity may be an excellent beneficiary of an IRA.

## Chapter 7

# PRESERVING THE FAMILY LEGACY: Summary and Affirmation

*“A Legacy is the footprint we leave on the sands of time.”*

—Anonymous

### **Opportunity—Achieved or Lost?**

An individual legacy is a very personal thing, filled with significance for the person who contemplates life going on without his or her presence. A family legacy is even more significant and all the more powerful.

Professional estate-planning professionals—attorneys, C.P.A.s, financial planners, life insurance agents, trust officers, stock brokers, and charitable-giving officers—all have disappointing stories of families who possessed a potential for creating or preserving a wonderful legacy and who never met that potential. More often than not, that failure occurred by omission rather than commission. The reasons range from “not getting around to it” or the preoccupation with priorities other than spouses or family members to the goal of keeping control until the very end (or even trying to control from beyond). In the end the reasons become irrelevant.

### **Surmountable Barriers to Planning**

The Baker family, however, is a different story. Blessed with success and with love and caring for one another and their community, Bob and Sue Baker have charted a course that took them into unknown waters. They could not have predicted where their journey into business succession and estate planning would take them. Like many, they began with doubts and fears. What if their son Jim was simply just too immature to take over the family business? What if their older son, Joe, kept distancing himself from the family? And what if their worst fears about their middle child, Jane, proved to be true, and she and her children lived under the specter of a painful marriage?

How were Bob and Sue to sculpt a family legacy out of these uncertainties?

Had they become preoccupied with the family “problems” that seemed to be barriers to creating a future for themselves, Bob and Sue most likely would have done nothing. Bob would

still be waking up nights, worrying about the business decisions facing Baker Pumps. And Sue would be lying awake worrying about Bob's health and wondering when, if ever, she and Bob would have the time together they had been promising themselves for forty years. The reasons *not* to do something come all too easily.

Bob and Sue took a different approach, however. While not having all the answers and while not knowing exactly what to do, they took a positive course of action. They chose to make an appointment with their attorney, Fred Scott, to move forward, out of their uncertainty. They did so, motivated by their own needs and their wishes for their own future together. They had what at that point was only the bud of a legacy that was to bloom later. Their commitment to their own well-being, however, was stronger than their uncertainties or their fears. The appointment with Fred Scott was a decision that opened a door that would lead them to create a legacy they neither anticipated nor ever imagined.

## **The Solution-Oriented Approach**

Their choice of Fred and his recommendation to work with family communications specialist, Bill Smith, turned out to be fortunate. Both advisors are consummate professionals with extensive experience and expertise with families in the Bakers' situation. In addition, they share a philosophy of setting goals, gathering pertinent resources together, and then applying them to the clients' envisioned goal(s). Both also believe the Baker family has within itself the resources to reach its goals, no matter how unfeasible or unrealistic those goals might seem at first. Fred and Bill see their roles as facilitators, roles that are by no means casual or passive. Instead, they actively listen to the Baker family members and point out strengths—including solutions already in the making—and celebrate with the family the achievement of their goals, both large and small.

In this process, the Bakers discover in one another strengths and capabilities of which they were not aware. Joe learns of his father's original desire for him, not Jim, to run the family business. Bob learns of Jim's business capabilities that Bob had no idea he possessed. He and Sue take new-found pride in Jane's assertiveness and desire to be part of the family business. They also realize that her own capacity for devotion and loyalty, rather than being a weakness, is truly a strength for the role she will play in her parents' estate plans. Jeff learns that in spite of his differences with his wife, his in-laws are not against him. Jill sees the deep capacity for love and caring her husband has for her, their child, and their future. And Jennifer realizes that while planning for your family without you may be much more difficult, it is necessarily a task to be performed if you truly care about your family. They discover and activate inherent resources as they learn to create solutions.

## **The Emphasis on Relationships**

These realizations on the part of the family members are not the traditional ingredients of a

typical estate or business plan. More often the phrases, CRATS, CRUTS, GRATS, and QPRTS come to mind. The Bakers do adopt some of these vehicles as part of their planning—not from a predesigned plan from their attorney but from the interaction of the parents with their children in conjunction with their attorney and succession advisor. *Relationships are the vehicles of the estate- and business-succession planning process.* Resource empowerment is the fuel that makes the relationships work. Traditional “vehicles” like CRTS become the end products of the process. In the business- and estate-planning process they may start as vehicles, but as the process evolves they are slowly sculpted, discussed, considered, and eventually finalized throughout the family retreat. This brings the reader full circle to the definition of estate planning introduced in the Preface: *estate planning is a series of emotional decisions formalized in a logical plan created by a professional advisory team to optimally ensure the considered feelings, beliefs, and goals of the testator.*

## **The Baker Estate Plan Summarized**

It will be helpful to review the decisions Bob and Sue ultimately make based upon the input from their family. Keep in mind that each decision point also involves the gradual creation of the Baker legacy, though that is not necessarily the direct intention of Bob and Sue at that particular time.

A summary of the final plan can be found in Appendix C.

To begin with, Bob and Sue each establishes separate revocable trusts, pourover wills, durable powers of attorney, and living wills. Upon the death of the first spouse, credit shelter trusts will be established to protect the first \$5.0 million of assets from estate tax by using the first spouses’s unified credit. Therefore, in 2012, Bob and Sue can pass \$10.0 million worth of assets to their family free of estate tax, less any unified credit that they may have used in the meantime in making gifts.

Upon the death of the first spouse, any assets in excess of \$5.0 million, assuming a death in 2012, will pass to a QTIP trust that will provide all income to the surviving spouse plus invasion powers in the corporate trustee to invade the trust for the survivor’s health, education, maintenance, and support. This trust will provide significant benefits to the survivor, will qualify for the marital deduction, and will also provide protection for the survivor in terms of investing and future expenditures of the funds. Both the credit shelter trusts and the QTIPs will be established in such a fashion so as to ultimately provide a protective trust for Jane and a generation-skipping trust for Joe. Note that in the Bakers’ case, as soon as they begin to plan for the next *generation*, they are preserving their legacy.

Each separate revocable trust is funded with half of the stock of Baker Pumps and some marketable securities. An aggressive gift-giving program will commence immediately to begin giving stock in Baker Pumps, Inc. to Jim and his children, and equalizing gifts will be made to Jane and Joe and their children in trust using other assets such as limited partnership interests and



marketable securities. Upon the last to die of Bob and Sue, the remaining shares of stock in Baker Pumps will pass outright to Jim. The Bakers may have a heightened sense of legacy because of their family business. Unlike other assets, a business requires a level of daily personal involvement and effort to maintain. Also, a business has a life-span of its own, and it is natural to expect a business to survive across generations. The challenge of planning for the business's future is a natural entry into creating a legacy for Bob and Sue.

Bob and Sue's marital home will remain in both names as tenants by the entirety, and upon the death of the second spouse will pass to trusts for Joe and Jane. Again we see a level of personal investment in an asset—perhaps obvious because it is the family home—yet it is this sense of emotional ownership that is an important ingredient in the building and the preservation of a legacy. The highly appreciated, low-basis securities will be used to fund a charitable remainder trust. Bob and Sue are the payment beneficiaries for life, and at death the remainder interest goes to the Goodall Clinic. Since Bob is grateful to Dr. Henderson of the Clinic for saving his father's life, we see the impact a previous generation has upon the Bakers. Bob very much believes his business success is tied to learning business at his father's side in the family grocery store. He has a deep bond with his father. This has deepened since his father survived a heart attack and open heart surgery. The discussion of Bob's feelings for his father stimulates Sue's feelings of wanting to help her church and leads to Jane's suggestion of commemorating her mother's parents with a plaque on the new educational wing. That the suggestion comes from Jane, as a granddaughter, is a strong statement about the Baker family ties of loyalty to one another. This is the informal, emotional, inter-generational legacy at work, which eventually ends up in a formal process that ties the three generations even closer together and which ultimately builds the foundations for bonds to the fourth.

The balance of the securities that are not highly appreciated will pass at the death of the second spouse to the trusts for Joe and Jane. The commercial building housing Baker Pumps is to be used to fund a family limited partnership with Bob and Sue as the shareholders of a new "S" Corporation, which will serve as the general partner. The limited partnership interest will also be owned initially by Bob and Sue. Any remaining interest at the death of the second spouse shall be transferred to the trust for Joe and Jane. As part of the gift-giving program, limited partnership interests will be given to Jane and Joe and their children starting immediately. Just as the business-succession decision to have Jim manage Baker Pumps creates a two-generation legacy, creating a family limited partnership with the commercial property has the same effect. The personal involvement of all three children in the future of Baker Pumps creates a climate of ownership as well as accountability. Because Bob and Sue have made their gifts in the spirit of justice and cooperation, this is the understanding the children inherit as far as their responsibility for owning the business assets as well.

The Keys property will be transferred to a qualified personal residence trust. Bob and Sue will have full use of the Keys property for ten years, at which time it will pass equally to all three children. The legacy here once again is not just of the passing of an asset but of an asset with a high level of emotional involvement on the part of all parties. The Keys property is highly symbolic for the Bakers. It is the sanctuary in which the Bakers gather as a family, removed from

the rest of the world. It is a place of leisure and relaxation where bonds are forged and deepened. In addition the Keys retreat home is symbolic of the family's commitment to the environment. The Bakers do not want the property owned by an outsider, nor do they want its special aura changed in any way. It is "a magic place," as Jane says. It is part of a long-standing Baker tradition. Tradition and legacy are inseparable.

Legacy does not only mean looking to the past, however. It can mean forging new relationships to continue old values into the future. Bob's IRA provides the means to accomplish this. It will remain in his name at this time, and upon his death the beneficiary shall become a charitable remainder unitrust for the benefit of Sue during her life. Upon her death the remaining IRA benefits will pass to the University of the Southeast, thus avoiding all estate and income taxes on the IRA benefits at Sue's death. This decision confirms a sense of nostalgia for the Bakers, since so many of them attended the University. Yet by connecting with an institution through a charitable gift, Jim is building bridges for the next generation of Bakers and Baker Pumps as well. There may well be a degree of self-interest and of business-interest in this transaction for Jim, and this is perfectly normal. Charitable gifts at one level involve a mutual exchange—of goodwill, of resources, of affiliation, and even of mission. Using the IRA for a charitable remainder trust to benefit the University of the Southeast may have mutual benefits for Baker Pumps and for the university that cannot be envisioned now. This is one of the greatest effects of a family legacy, enhancing not just individual and family bonds and interests but also those of groups and institutions that make up the social fabric.

Finally, Jim will immediately purchase a \$1,000,000 second-to-die insurance policy on his parents' lives to assist in the payment of estate taxes on his inheritance of Baker Pumps, Inc., stock.

### **An F.O.B. (Family-Owned Business) Legacy**

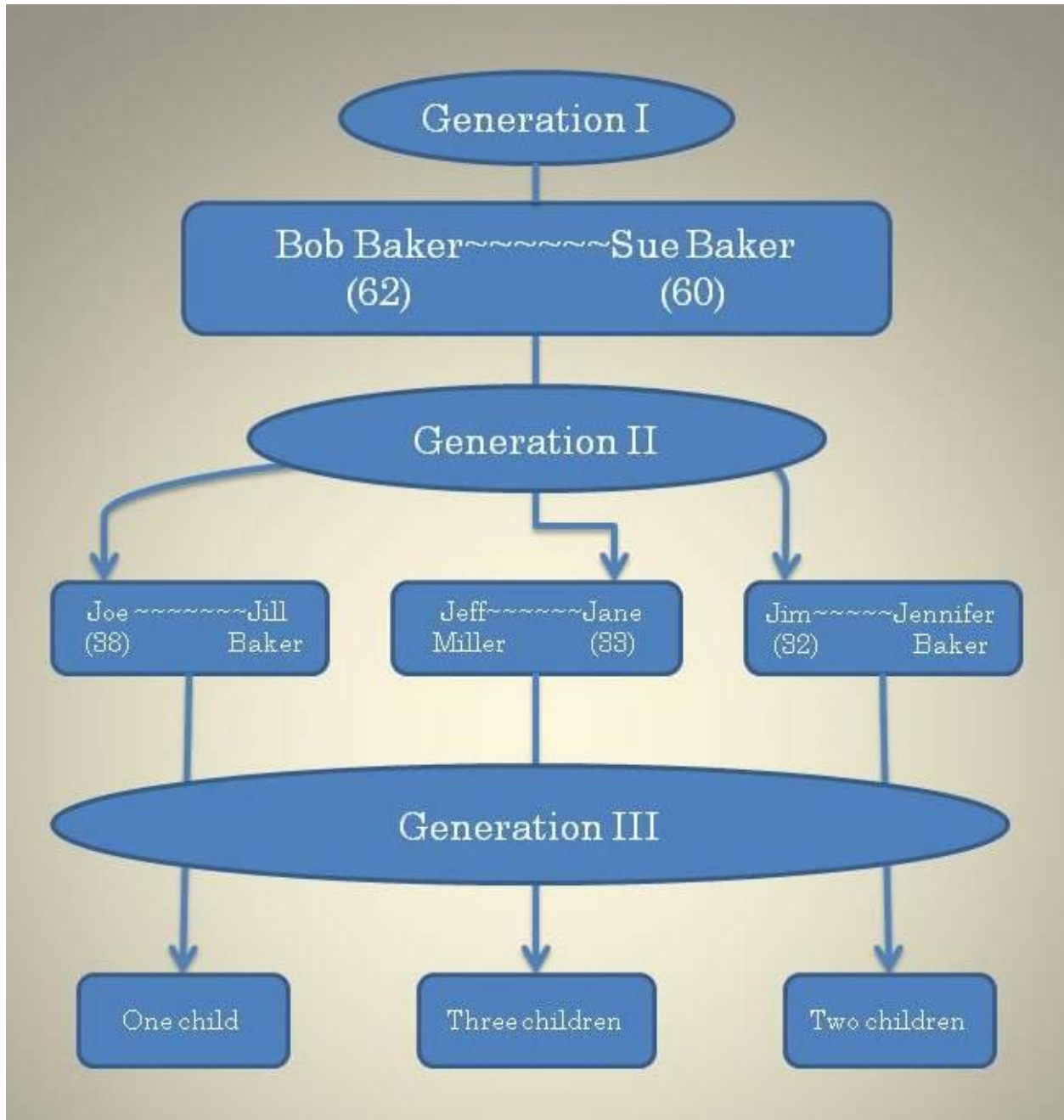
The Baker family legacy began as a concern for the successful business succession of Baker Pumps and has grown into a multi-generational affirmation of the entire Baker family. "Legacy" in this context has grown to mean more than the relationship between parents and children. It has come to include, actually, four generations of Bakers, from Bob's and Sue's parents to their grandchildren. The Baker legacy also includes all that Baker Pumps has meant to Bob for thirty years—his striving for initial survival, then maintaining it, and finally creating a cross-generational enterprise. "Legacy" for the Bakers also has come to mean a set of values in which people genuinely care and look out for one another. This is rooted in Bob and Sue's relationship with one another but was demonstrated in the retreat time and again in various interactions—including Bob's candor with Joe and with Jim about his abilities, and Sue's candor with Jane about her marriage. It is evident in Joe's consideration of his wife's future without him, in the respect shown to Jeff, the son-in-law, by the rest of the family in spite of his troubled marriage with Jane, and it is evident in the gratitude and generosity Bob and Sue shared with the Goodall Clinic, First Church, and the University of the Southeast in their charitable gifts. Finally, the Baker legacy is exemplified thoroughly by the family commitment to the Keys home and to the

role they wish it to play in keeping the Baker family heritage alive.

The Baker family legacy is grounded in years of life together. There has been turmoil, differences, conflict, and resolution. The Bakers are fortunate in their love and respect for one another. Whether or not other families enjoy this devotion, family ties provide the motivation to preserve a sense of identity and legacy. Professionals who have the opportunity of working with a family like the Bakers are twice blessed—first, to be afforded the opportunity to participate in a living legacy that with professional assistance will grow and thrive; and second to witness the true makings of a legacy, not in numbers and graphs, but in the lived experience of a family culture at its best, focused on its goals and headed toward triumph.

## APPENDIX A

### BAKER FAMILY TREE



## APPENDIX B

### BAKER FAMILY ASSETS

Baker Pumps Stock	\$6.0 million
Commercial Property	\$2.0 million
Residence	\$2.0 million
Vacation Home	\$2.0 million
I.R.A.	\$1.0 million
Brokerage Account	\$7.0 million
<b>Total</b>	<b>\$20.0 million</b>

## APPENDIX C

### THE BAKER ESTATE PLAN

#### **Baker Pumps, Inc., Stock (\$6.0 million)**

Bob transfers 50% of company to Sue immediately. Gifts during life to Jim and his children, remainder upon death to Jim.

#### **Commercial Building (\$2.0 million)**

Family Limited Partnership with gifts of limited partnership interests during life; plus upon parents' death, to trust for Joe and Jane, and their children.

#### **Residence (\$2.0 million)**

Upon parents' death, to trust for Joe and Jane, and their children.

#### **Vacation Home (\$2.0 million)**

Qualified Personal Residence Trust (QPRT) for 10 years for Bob and Sue, ultimately to Joe, Jane, and Jim.

#### **Bob Baker's I.R.A. (\$1.0 million)**

Upon death to Charitable Remainder Unitrust (CRUT), with payments to Sue for life, remainder to University of the Southeast.

#### **Securities (\$7.0 million)**

\$5 million of low-basis, highly appreciated securities to Charitable Remainder Unitrust (CRUT) with payments to Bob and Sue for their lives, remainder to Goodall Clinic. Balance to trust for Joe and Jane, and their children at Bob and Sue's death.

#### **Life Insurance**

\$2.0 million second-to-die life insurance purchased to pay estate taxes.

## APPENDIX D

### UNIFIED FEDERAL GIFT AND ESTATE TAX

	2011	2012	2013
Top Estate Tax Rate	35%	35%	55%
Estate Tax Exemption	\$5.0 million	\$5.0 million	\$1.0 million
GST Tax Rate	35%	35%	55%
GST Exemption	\$5.0 million	\$5.0 million	\$1.0 million
Top Gift Tax Rate	35%	35%	55%
Gift Tax Exemption	\$5.0 million	\$5.0 million	\$1.0 million

## APPENDIX E

### BAKER TEAM OF PROFESSIONAL ADVISERS

Estate Planning Attorney	Fred Scott
Family Communications Specialist	Bill Smith
Financial Planner	Susan Jones
C.P.A.	Joel Leventhal
Insurance Agent	Phil Johnson
Trust Officer	Mike McKinley

Note: Because of a long and successful business relationship, the lead professional in the Bakers' case is their estate planning attorney. In other cases, relationships will dictate that a different professional will serve as lead advisor. Regardless of which professional initiates the estate planning or business succession activity, or which one leads it, the key to a successful team approach is:

1. A high level of competence among all team members.
2. A high level of cooperation among them accompanied by mutual respect.
3. The responsibility for coordination, deadlines, and service quality ultimately must sit on the shoulders of one team member.



## **SEMINARS AND WORKSHOPS**

**William A. Snyder, J.D., LL.M.**  
**Tim Bachmeyer, M.A., Ph.D.**

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We are dedicated to helping families thrive who own small businesses. To that end, we offer a menu of services for business owners, their family members, and their professional advisors. For details, contact us at the address or phone number above.

**Business Succession and Retirement Planning for the Family Owned Business:** Examination of the issues an entrepreneur and his or her family face in passing on the family business. Relationship, communication, legal, and financial issues are addressed. For family members and business advisors. Dr. Bachmeyer and Mr. Snyder.

**Communication Strategies to Enhance Family Cooperation.** Within a family business, interaction between generations is always intensified. The potential for resolution of differences and mutual satisfaction, however, is also higher than the temptation to let differences fester and diminish the business. Specific communication techniques taught and practiced. Dr. Bachmeyer

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Individual counsel is also provided on operational business issues, such as executive assessment and evaluation, and CEO coaching.

## **ABOUT THE AUTHORS . . .**



### **Tim Bachmeyer, M.A., Ph.D.**

Dr. Bachmeyer grew up in a small business family in Kalamazoo, Michigan. He left to attend Yale, where he received his B.A., and the University of Chicago, where he received his advanced degrees. He conducted a private practice in family and group psychotherapy while teaching psychology at several Milwaukee area colleges. He specialized in working with Fortune 500 executives and their families, as well as several Executive MBA programs. Since 1983, he has been a charitable gift planner, helping families around the country achieve their legacy objectives. The originator of a psychological profile, “The Millionaire Mindset,” he consults on strategies to cultivate high net worth individuals. He is a member of the National Committee on Planned Giving.



**William A. Snyder, J.D., LL.M.**

Mr. Snyder grew up in a small business family in upstate New York. He holds a B.A. from Hobart College, a J.D. from the University of Florida Law School, and an LL.M. from the University of Miami Law School. He has conducted an estate planning practice in Davie, Florida, for more than 40 years, specializing in small businesses. A member of The Florida Bar, he is Board Certified by The Florida Bar in wills, trusts and estates, and is rated AV by Martindale-Hubbell. He is an adjunct professor at the University of Miami School of Law graduate program in estate planning. He was recognized for three years as one of *Worth* magazine's "Top 100 Attorneys" in the United States, named in 2007 through 2011 in *The Best Lawyers in America*®, and was listed in 2006 through 2011 in *Florida SuperLawyers*®. He is a Fellow in ACTEC (American College of Trust and Estate Counsel).