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Entrepreneurs: You Need an Estate Plan to Protect Your Spouse and Business

While it's always important to have an estate plan in place to ensure your wishes are met and to protect your loved ones, it's especially crucial if you own a business that is the family's main source of income or is a significant portion of your overall estate. It will prevent a lot of worry and misunderstandings if couples who own businesses are open about their concerns regarding how the loss of income from a business might affect them.

Let's say one partner owns a very lucrative business. The stay-at-home spouse who does not generate income may have concerns about how she will be provided for after a death. In this case, it would be important for the spouse to know: "What happens to the business and the income it provides should you pass away? Am I receiving any portion of the business when you pass or do I become owner of your share?" An estate plan is critical in such situations because a lack of a plan for a business owner could leave business partners and/or family members in turmoil and the business itself in chaos.

If you own a business, there are three key issues to consider and discuss with your spouse to create a plan that protects them and the legacy you've built: the role of the remaining spouse, a buy/sell agreement, and the division of business assets.

THE ROLE OF THE REMAINING SPOUSE

Many of the concerns that come about when one member of a married couple owns a business are strongly contingent on whether the business is owned outright.

When a business owner dies, the remaining spouse must handle both grieving and managing the financial repercussions of the spouse's death. When a business partner or multiple partners are involved, and the couple did not own 100 percent of the company, the issues become much more multi-layered. This is especially true if the remaining spouse wants to be involved in the business in some capacity. In this case, there are two main questions to consider: Does the surviving spouse wish to, or have any ability to, assume a co-management role? Secondly, does the external business partner want to be in a partnership with the surviving spouse?

No matter what you decide, you should also have the same kind of frank conversation with your business partners about developing a plan to protect your loved one's interest in the company. It will ease a lot of anxiety for your spouse and family, as well as your business partner, if a plan is in place. A well thought-out business succession plan will ensure a seamless transition amongst all the parties while allowing the business to continue to operate efficiently.

In most cases, even if a couple owns 100 percent of the business, the surviving spouse may not want to operate the company. It's crucial for the spouse who doesn't run the business to be frank and feel comfortable saying, "I'm worried about managing all this if you go before me." For these reasons, it's essential for couples — and their business partners — to anticipate and discuss possible ownership and management issues so their visions for the running of the company in the event of a death are aligned.

A BUY/SELL AGREEMENT

A buy/sell agreement takes into consideration what happens if the business owner dies or wants to retire. It may seem like common sense that a business agreement covering contingencies such as death or retirement should be an integral part of building a company. However, it's common for business owners to put off such tasks until long after the company is up and running.

A buy/sell agreement is as much about protecting your family as it is about protecting your business partners and your company. Not having some form of a business succession plan or management agreement in place could prove extremely difficult. Let's say that your spouse has a 50/50 business partnership with someone. A worst-case scenario would be that the business has a pending government contract, but because of the demise of one of the partners, the other partner cannot act on it alone due to a pre-established rule that says both partners must agree to new client contracts. Without a plan in place to detail what happens operationally when one partner passes away, the company's future could be in jeopardy.

In a worst-case scenario without a succession plan in place, the surviving spouse who does not have an understanding of the business declines to sign the government contract out of an abundance of caution. Next thing you know, the contract lapses, potentially jeopardizing the business relationship.

These and many other potential complications can be avoided with a comprehensive agreement that addresses how and by whom the company will be run if when one partner dies.

DIVISION OF BUSINESS ASSETS

Even when a company is solely owned by one person, how to fairly divide the assets of a business among family members can be a complicated issue. For many families running a business, it's often the case that much of their accumulated wealth is derived from that business, which then gives rise to many questions: If only one or two of the family members work in the business, who inherits the business? Do you divide it equally among all or do you give the business to the family members who are working in it? If you give the business to some family members, do you then provide cash, bonds or securities to the other family members to offset the business interest?

Even if you have a business succession plan in place, it's not enough to simply hand over the company to the family members most actively involved in the enterprise. That could cause an inheritance imbalance and result in friction between estate beneficiaries. Typically, that's when we see insurance policies come into play. For example, the business might be worth $5 million, so the parents buy a $5 million policy to equal the value of the business. Thus, child one and two inherit the business and child three and four inherit the insurance proceeds. Please bear in mind, this is not the solution for all circumstances. An estate planning expert is best suited to advise you on how to remedy the potential imbalance of assets.

HOW TO PREPARE YOUR BUSINESS

Ownership of a business can add numerous complications to estate planning. It's a good idea to speak with a professional to ensure all possible family, partner and business-related concerns are covered in your will and estate plan. It's also especially critical to speak with your spouse to ensure you're both on the same page when deciding what will happen to the business when you pass away.

To learn more contact your Financial Advisor or CNR Senior Investment Consultant or Portfolio Manager, visit us at CNR.com, or email us at citynationalrochdale@cnr.com.

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