



## WHEN BUSINESS GETS PERSONAL

THE CHALLENGES OF PASSING THE FAMILY BUSINESS TO THE NEXT GENERATION

BY MICHAEL LAURENCE

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You've spent a lifetime building your company into a success. Now as you start to look toward retirement, you're considering letting your children or other family members take over. This is when business really gets personal.

"It can be the ultimate management challenge," said Jason Smolen, business attorney and co-founding principal of Smolen Plevy, a Vienna, Virginia law firm. Smolen says he's seeing a dramatic shift as aging baby boomers approach the end of their careers and prepare for the next phase of their lives. Studies bear him out. A MassMutual/Raymond Institute American Family Business Survey shows about 40% of family businesses expect the leadership of their companies to change this year. More than half of family businesses expect a leadership change by 2013.

But here's the problem. Studies show more than 70% of family-owned companies don't survive the transition to the second generation. Smolen uses a French expression to characterize the difficulty of passing the family business to the children: "Après moi le déluge," meaning, "after me, come the floods."

There are multiple complications and issues that can derail the process. Among them:

- Who wants the business? Is it one of your children, all of them, sons or daughters-in-law or other relatives?
- Will those immediate relatives who don't plan to participate in the business still expect some kind of compensation?
- Who is driving the process? Is it the parents' idea, or is it being pushed through by the children/next generation?
- Will the parents have enough to live on once they turn over the business?
- Does the person taking over have enough experience and ability? Will they have enough time to develop the necessary business skills?
- How will the taxes be handled?
- How can we stop jealousy and in-fighting from grinding the transition to a halt? Will spouses help or harm the process?

Too often, a lack of comprehensive and long-term planning is the culprit, especially when the owner dies suddenly. In that situation, a valuable company could lead to a large tax bill. The heirs are going to have to pay it, and if there's not a lot of cash on hand, the company may have to be gutted, or sold. Without a succession plan in place, many companies suffer an early and expensive demise.

Smolen says another problem is planning that comes from the bottom up. "The children are driving the process, forcing their parents to hand over the business, often too soon," Smolen said. He warns that when the children push the plans

there's a sense of entitlement, often undeserved. "The children are worrying about what's best for them, while the parents are trying to keep their kids happy," Smolen said. "Worse, the parents may not be ready—either psychologically or financially-- to hand over their company. What are they going to live on if they retire too early?" Smolen strongly advises the parents and the next generation have separate attorneys.

Smolen, a noted expert on business succession law, said planning can never start too soon. "Five years is good, ten is better." In addition to establishing an operating system for the company to move forward, it also allows time for proper gifting—which is one way to start turning over the financial reigns of the company. Both parents can gift up to a million dollars apiece in a lifetime plus make annual gifts up to \$12,000. Smolen says it's important to begin gifting early, because if the value of a company increases—which you hope it will—parents need time in order to gift enough away.

Even with plans in place, the process will continue to be a tightrope walk. Smolen strongly suggests consulting with experts about tax and succession planning—which can lead to a much more successful transfer of ownership. There are three key goals to the process: making the succession legal, tax efficient and sensitive to family harmony.

On the topic of harmony, Smolen suggests keeping the children or relevant family members involved in the process. "While you know what you're giving, you don't always know how it's being received," Smolen said. "It's best to ask, and make sure the next generation is onboard in the arrangement."

In addition, Smolen suggests examining the strengths and weaknesses of all your possible successors to make sure the business goes to the right person or people. And, proper planning gives you time to train and work with your successor.

The business you spent a lifetime building is, in many ways, "your other child." A good succession plan can ensure that you have the funds you need to retire and that the business you have built continues to thrive in the hands of the next generation.

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