



## PALMER CASE STUDY: BUSINESS SUCCESSION AT ITS BEST

Thirty years earlier an aging businessman transferred the stock of his small family business, a manufacturing company, to his two sons who were both in their early 20s. This small manufacturing company had struggled over the years, but the vision and innovation of the father provided a great opportunity to substantially grow this small family business to multiples of what it was. The transfer of the stock to the boys was not legally or financially a challenge because the value of the business at that time was still quite small.

What typically is a great challenge for a founder/owner is to emotionally take his “hands off the wheel” of the business and let his sons take the business and run with it. And run with it they did.

Over the next several decades the two brothers grew this small family business into a multi-million dollar company that distributed its products literally all over the world. They went from a mere handful of employees to having hundreds of employees. It expanded from working out of the family barn to a huge manufacturing facility of tens of thousands of square feet.

Now, decades later, as these two brothers were approaching the end of their own business careers, they faced the same business succession planning decisions that their father had faced decades earlier. But what had been a simple business transfer and succession plan for their father was anything but simple for them.

Two major challenges faced these brothers: (1) which children would step into the leadership and ownership of the company going forward, and (2) how would they get the value of the business to their heirs without facing millions of dollars in crippling capital gains, gift or estate taxes on the transfer.

Step 1 was to identify which children with the gifts and abilities as well as the passion for the business could be groomed to take over the leadership of the company when the brothers were ready to turn over the reigns of the business to the next generation. Each child was asked at a family meeting if he/she had any interest in the leadership of the company going forward. Some who were stay-at-home moms or already had established careers indicated they did not have an interest in running the family business. Those who did indicate an interest were given assessments to identify their giftedness. Several personal interviews were conducted with each of these family members.

Because the two brothers were Christians, they wanted those who would lead the company in the future to feel a real sense of divine calling to lead the company going forward. As it turned out, two sons of one of the brothers were identified as being exceedingly gifted, called, and anxious to take this already successful company to the next level.

Once these two brothers were identified as the family members who would run the company for the next generation an extensive, multi-year, training program was created to expose and teach these young men every aspect of this multi-department business.

The second step was to create a wealth transfer plan for each of these two families. Several challenges existed that had to be addressed. First, how to get the business to these two sons without paying millions in capital gains, gift or estate taxes. Second, how to get the other children an appropriate inheritance since the vast majority of both brothers' wealth was in their company stock. Third, how to arrange the transfer so when the brothers transferred the stock, they would still have enough to provide for an ongoing stream of income for their retirement.

After considerable strategy planning it was determined that the most effective way to transfer the stock was to utilize a *Charitable Stock Buy-Out Plan*. The first step in the plan was to transfer a minority interest of stock to each of the two boys so that they were now minority owners of the company. Then, each brother at the appropriate time would transfer their stock into their own Enhanced Income Trust (EIT).

Next, the company would offer to buy the stock from the trust on a 10 year note using its after-tax company profits and pay the note off. Because this trust is tax exempt, it pays no capital gain taxes on the sale of the stock, leaving 100 percent of the sale proceeds in the trust to be reinvested. Going forward, each brother and his wife would receive a regular, annual income from their respective trusts providing them with more than sufficient annual income for all their lifestyle needs, their charitable giving, and their gifts to their children.

Once both brothers had transferred their stock to their EITs and it was all purchased back by the company and retired, the two sons owned all the outstanding shares of stock and the ownership of this multimillions dollar company was transferred to the next generation – tax free! Their respective multimillion dollar Enhanced Income Trusts would terminate on the death of each husband/wife, and their assets would be given away to Christian ministries and causes the family wished to support.

The final component of the wealth transfer plan was to provide an adequate inheritance to the other children who were not taking ownership of the company. The parents wanted these children to receive part of their inheritance during their lifetime and the balance once both parents went to be with the Lord. The lifetime inheritances would come from the excessive cash flow of each brother's Enhanced Income Trust. These lifetime gifts would be tax-free, using annual gift exclusions and their lifetime exclusions. Their testamentary inheritance would come through a Wealth Replacement Trust which they would also receive tax free once both parents passed on.

The bottom line of this very sophisticated plan was (1) the brothers were able to successfully transfer their multimillion dollar business on to the next generation completely free of any capital gains, gift or estate taxes; (2) it provided both brothers a lifetime income stream once they stepped away from the business; (3) it provided the other non-business owner heirs an inheritance that the parents deemed appropriate; and (4) this plan helped the two brothers give away about 100 million dollars during their lifetimes and beyond to Christian ministries and causes that they deeply cared about. This case study demonstrates the power of comprehensive and integrated creative planning. It truly is an excellent example of business succession planning at its best!

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## **ABOUT THE AUTHOR — E. G. “JAY” LINK**

Jay Link, Director of Stewardship Planning at Taylor University, spent 35 years counseling Christian families to build customized Master Stewardship Plans. He is an author, a mentor to hundreds of financial advisors and attorneys, and started his career as a pastor. His passion is helping Christian families use all the Lord has entrusted to them for Kingdom-building purposes.