TAX AND WEALTH ADVISOR ALERT: HOW DOES LIFE INSURANCE WORK WITH AN ESTATE PLAN?

We must always expect the unexpected. We can be careful and prudent in our daily lives, but there are certain things that are out of our control, like death. In the event of your untimely death, are you able to provide ongoing support to your loved ones and important causes? By securing life insurance and establishing a comprehensive estate plan, you can help protect your family and loved ones and support your charitable causes after your death.

What is Life Insurance?

Life insurance is a contract with an insurance company that provides a sum of money to a designated person or entity upon the death of the insured person. Some policies also contain provisions that permit a payout upon a specific event, such as a terminal or critical illness. Buying life insurance is a common way for people to plan for the future of their families, loved ones, businesses, or other causes. It is important to understand what type of life insurance suits your needs.

What are the Different Types of Life Insurance?

There are two main types of life insurance that an individual can purchase: term life insurance and permanent life insurance.

- Term life insurance – This type of life insurance provides a death benefit upon the death of the covered insured during a specific, fixed period, often 1 to 30 years. The policy will pay out benefits to the designated beneficiary if the insured dies during the policy's term. Term life insurance is often purchased by individuals who want coverage for specific reasons in the event of their death, such as taking care of minor children or paying off a mortgage. Term life insurance is more affordable than permanent life insurance, as it only offers benefits for the term of the policy. If you have a small estate that is simple to manage, then term life insurance might be your best option.
- Permanent life insurance – This type of insurance provides a death benefit upon the death of the covered insured and a cash value that the covered insured may be able to access during their life. Common forms of permanent life insurance are whole life, universal life, variable life, and variable universal life insurance. Permanent life insurance is commonly purchased by individuals who have large estates that are complex to manage. While permanent life insurance is more expensive than term life insurance, its potential benefits can be much greater. If you have a special-need heir, large assets that are difficult to divide, or high estate taxes that will burden the beneficiary, then permanent life insurance might be your best option.

For both types of insurance, it is important to pay the premiums. With term life insurance, the policy typically lapses if you fail to pay a premium and your beneficiaries will obtain no

benefit upon your death. With permanent life insurance, the contract may provide different choices if you fail to pay the premiums.

Make sure to work with an experienced estate planning attorney and your insurance agent to evaluate your situation and determine what type and level of insurance are best for you and your loved ones. Your current decisions can benefit future generations if you plan appropriately.

What are the Most Common Benefits of Having Life Insurance?

There are several important benefits that can be realized with the appropriate type and level of life insurance. Some of the most common benefits of life insurance include:

- Taking care of loved ones
- Maximizing wealth
- Paying off mortgages or other debts
- Securing a long-term legacy
- Protecting a business long-term
- Putting wealth into important causes
- Leaving a gift to charity

It is important to secure a policy that meets your long-term goals. Make sure you consider your choices so your plan is the best fit for you.

What is an Estate Plan?

Estate planning is the process of thinking about what will happen to your money, property, and other possessions after you die. Estate planning can determine how your affairs will be handled in the event that you become unable to care for yourself. Estate planning may also include planning for the long-term succession of a business. A goal of estate planning often is to minimize the amount of taxes and other expenses that arise upon death. Your personal goals and wishes should drive the type of estate plan you create. There are different mechanisms to develop a comprehensive estate plan, which can include:

- Will
- Trusts
- Powers of appointment
- Determination of property ownership and retitling of property
- Gifts
- Powers of attorney

A comprehensive estate plan should be tailored to your needs and your desires and should not be a cookie-cutter form document.

How Can Life Insurance Work with an Estate Plan?

The appropriate life insurance policy can be a significant part of your estate plan. Often, individuals simply designate a family member as the beneficiary of a life insurance policy without considering their overall estate planning goals. This can result in unintended consequences such as unequal distribution to beneficiaries or tax implications. Designating the right beneficiary on any insurance policy is important to achieve your estate planning goals.

TAX AND WEALTH ADVISOR ALERT: IRS REMINDS INDIVIDUAL TAXPAYERS OF SEPTEMBER 15 DEADLINE FOR THIRD QUARTER ESTIMATED TAX PAYMENTS

The IRS has reminded taxpayers who pay estimated taxes that the deadline to submit their third quarter estimated tax payments is September 15, 2022. The fourth and final estimated tax payment for tax year 2022 is due January 17, 2023. Taxpayers not subject to withholding, such as those who are self-employed, investors, or retirees, may need to make quarterly estimated tax payments. Taxpayers with other income not subject to withholding, including interest, dividends, capital gains, alimony, cryptocurrency, and rental income, also normally need to make estimated tax payments.

In most cases, individual taxpayers need to make estimated tax payments if they expect their tax liability to be at least $1,000 for the tax year 2022, after subtracting their withholding and tax credits. Special rules apply to some groups of taxpayers, such as farmers, fishermen, casualty and disaster victims, those who recently became disabled, recent retirees, and those who receive income unevenly during the year.

To compute estimated tax, individuals must determine their expected Adjusted Gross Income (AGI), taxable income, taxes, deductions, and credits for the year. While calculating their 2022 estimated tax, it is helpful for taxpayers to use their income, deductions, and credits for 2021 as a starting point. Taxpayers can avoid underpayment penalties by making payments of at least 90% of the tax expected on their 2022 income tax return, or by making payments of at least 100% of the tax shown on their 2021 income tax return. The IRS may waive such penalties for underpayment due to unusual circumstances, but not willful neglect.

Additional information regarding individuals that need to make Federal and Wisconsin estimated tax payments and how to make such payments can be found here. For questions or further information relating to estimated tax payments, please contact Attorney Britany E.

Morrison.

AN EDUCATIONAL BUSINESS SERIES FOR SUCCESS: DEFINING HOW OWNERSHIP INTEREST(S) CAN BE TRANSFERRED IF ONE OR MORE OF THE OWNERS CAN NO LONGER OR DO NOT WANT TO CONTINUE IN THE BUSINESS

In our last article, we explained why setting in place an exit strategy when the time comes and minimizing the potential for conflict is important. In this post, we will be discussing how ownership interest(s) can be transferred if one or more of the owners can no longer or do not want to continue in the business.

PART 3 – DEFINING HOW OWNERSHIP INTEREST(S) CAN BE TRANSFERRED IF ONE OR MORE OF THE OWNERS CAN NO LONGER OR DO NOT WANT TO CONTINUE IN THE BUSINESS

Your business is soaring along, meeting or exceeding all projections and expectations, and then suddenly one of the owners wants to pull out of the company. Or something disastrous happens and an owner simply cannot continue.

There is a myriad of reasons an owner may leave the business, including simply not having the passion to remain in it, but no matter what, you can and should be prepared. Whether your business continues to function at a high level or crumbles during this transitional period depends on how well you have anticipated situations that involve transfers of ownership interests. A well-drafted buy-sell agreement can help keep your business on track by defining how and when ownership interests can be transferred, and for how much.

Typical Buy-Sell Provisions

In many cases, the owner's interest must be sold back to the company, the remaining shareholders, or a combination thereof. A solid buy-sell agreement may be structured in several different ways and account for differing triggering events. In all cases, however, the buy-sell agreement should specify the value of the interest after the owners agree on the method of valuation.

In the most common scenario involving the death or disability of an owner, co-owners are required to buy the departing owner's share. Under what is commonly called a "cross-purchase plan," each owner would buy a life insurance policy on every other owner and pay the premiums, either personally or using business funds. The remaining owner or owners could then purchase the departing owner's interest from their heirs using the life insurance proceeds.

When the business itself will buy the departing owner's share upon the death of an owner, the buy-sell is funded with a life insurance policy bought by the business and on which it pays the premiums. The business would then use the proceeds of the policy to purchase the owner's share from their heirs.

In a situation in which a sole proprietor has handpicked someone to take over the business, a one-way buy-sell agreement may be the best choice. In this case, the chosen person—whether it is an employee, child, sibling, spouse, etc.—would buy an insurance policy on the owner and name themselves as the beneficiary. Premiums may be paid by the business or by the future owner.

Buy-sell agreements may also give the business the option to buy a departing owner's interest first. If the business declines, the option then moves to the remaining owners, but if they do not buy all the remaining interest, the business must buy it. This type of arrangement is called a "wait and see" plan because it allows the business to decide whether it makes good financial and tax sense to purchase the departing owner's shares at the time of the triggering event.

A buy-sell agreement may also provide remaining owners with a "right of first refusal," giving them the option to buy the departing owner's interest before it is offered to anyone else for purchase. This provision can help ensure that the remaining owners maintain a say in who their future partner will be, though it is not foolproof if the remaining owners do not have the funds available to buy the interest.

Remember, too, that owners do not always have equal shares in the business, and that means that separate buy-sell agreements may be in order. For example, a buy-sell for a minority owner may require them to sell their interest to the majority owner while one for the majority owner may prefer that a particular person, such as a child, take over their shares.

Overall, a comprehensive buy-sell agreement can cover many triggering events and scenarios while also keeping all current owners happy both during the course of business and in the case that the contract must kick in. The best buy-sell for your business will minimize potential conflict while also considering exactly what your specific business needs as well as potential tax consequences.

Check out our next article in our business series covering what types of protection needs to be considered in a transition.

If you have questions about your company's succession, please contact a member of our Estate and Business Succession Planning team.

OTHER ARTICLES IN THIS SERIES:

- An Educational Business Series for Success: Setting in Place an Exit Strategy When the Time Comes and Minimizing the Potential for Conflict
- An Educational Business Series for Success: Why Buy-Sell Agreements are Necessary Even if You Don't Plan to Sell Your Company Soon

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TAX AND WEALTH ADVISOR ALERT: ESTATE AND TAX PLANNING DURING MARKET TUMULT

The worldwide equity market tumult is creating some unique and unprecedented challenges. However, plunging asset values are presenting some rare opportunities in wealth planning that are often only seen once in a generation. Below are some strategies you may wish to incorporate into your estate and tax planning during this time.

Basic Estate Planning: Now, more so than ever, it is important to make sure your family is provided for in your estate plan. This means reviewing your current estate planning documents to ensure the principal documents are in order. Wills, revocable trusts, powers of attorney, beneficiary designations and health care directives should all be reviewed to ensure that these documents reflect your current wishes.

Make an Annual Gift Exclusion: You can make an annual tax-free gift of $16,000 per person (for married couples, a combined $32,000) that does not count against your lifetime gift tax exclusion (currently $12.06 million per person). Using marketable securities as the gifted asset when volatility is so high, and valuations are down, can offer you some extra stretch on gifts made now before valuations rise in the future.

Place Assets into Existing Irrevocable Trusts or Fund a New Irrevocable Trust: Like making an annual gift, funding an irrevocable trust with securities while valuations are low allows for more assets to be placed in the trust (when measured against the lifetime exclusion) and allows you to transfer more of your wealth tax-free.

Make Roth IRA Rollovers: The "cost" of converting a traditional IRA into a Roth IRA is

paying taxes now on the current value of the IRA, therefore, it is best to make these conversions when the market is down.

Tax-Loss Harvesting: Some may consider lowering their tax liability by selling a security now at a loss to offset gains from earlier this year or in the future. However, you should be aware of the wash-sale rules. The wash-sale rule states that when you harvest losses, you cannot repurchase substantially identical investments for 30 days. Even though you may have separate accounts with different advisors, the rule considers all accounts to be the same. Therefore, it is important to make sure that all your advisors are aware of the securities you are buying and selling.

Intra-Family Transactions: When asset values are low, wealth transfer planning techniques involving intra-family transactions, such as selling assets to your children or grandchildren, are very effective if the sold assets appreciate at a rate greater than the interest rate charged. When asset values recover, all the asset appreciation will be outside of your taxable estate and will be held by or for the benefit of your children or grandchildren transfer tax free.

GRATs: A grantor retained annuity trust (GRAT) is an estate planning vehicle that allows you to freeze the value of your estate while transferring any future appreciation to the next generation free of tax. With a GRAT, you transfer certain assets to a trust and retain the right to receive annuity payments for a term of years. The transfer of property to a GRAT constitutes a gift for gift tax purposes, but the value of that gift is only the value of the trust assets on the date of the transfer plus an assumed rate of return. Any appreciation of the assets more than the hurdle rate passes to the beneficiaries free of gift tax. GRATS are most effective when interest rates and market values are low. While the economy isn't currently experiencing low interest rates, it is experiencing low market values, which still makes it beneficial to set up a GRAT. For clients who have existing GRAT terms that are ending, it is probably beneficial to keep them going. Those without GRATs should strongly consider funding them in this current market climate.

CLATs: Those with charitable inclinations should consider a charitable lead annuity trust (CLAT). A CLAT works like a GRAT, however, a CLAT is designed for a charity to receive the annuity payments for a term of years, rather than an individual. At the end of the term, the balance of the assets remaining in the trust passes to the beneficiaries you indicate in the trust agreement. As with all the strategies discussed above, low equity values result in more assets passing to your intended beneficiaries free of transfer tax.

If you are interested in learning more about estate and tax planning during these unprecedented times, please contact Attorney Britany E. Morrison at O'Neil Cannon

TAX AND WEALTH ADVISOR ALERT: WHAT IS AN ESTATE PLAN?

We are often asked, “What is an estate plan?” An estate plan can mean different things depending on your unique personal and financial situation. We structure your estate plan based on many things, such as whether you are single, married, or divorced; whom you want your estate to pass to upon your death; and the complexity and makeup of your assets. Some individuals may need more estate planning, some may need less.

Here is a list of the typical documents we include in an “estate plan.”

Revocable Trust

People often come to us asking for a “simple” Will. However, a Will-based estate plan is not always the best choice. A “simple” Will now may cause beneficiaries significant cost and delay, later, when the Will gets probated. This is why we often recommend that our clients establish a “Revocable Trust.”

A Revocable Trust is a trust that you create during your lifetime and acts as the “centerpiece” of your estate plan. The Trust is designed to help you manage your assets during your lifetime and to designate who will receive your property upon your death. You are the “grantor” or creator of the Trust and serve as Trustee during your lifetime, so you still retain control over the assets in your Trust. The Trust is both completely amendable and revocable during your lifetime.

Upon your death, your trust property is divided and distributed to your named beneficiaries, often your children. A share for a beneficiary can either be distributed outright and free of trust, or it can be held in trust for that beneficiary’s benefit. A share held in trust can be useful for a beneficiary to protect from creditors and divorce, or if a beneficiary is a spendthrift.

Married couples often create a “joint” Revocable Trust together. A joint Revocable Trust is a useful tool to minimize taxes and effectively manage a married couple’s assets, before and after death.

A Revocable Trust is particularly useful if you have minor children, you own your own business, or you own real property in multiple states. The Trust also makes the administration of your assets more efficient if you become incapacitated.

Last Will and Testament

Even if you have a Revocable Trust in place, it is still necessary to have a Will. This is what we refer to as a “Pour-Over Will.” The Pour-Over Will serves a few important purposes. First, in the event that you fail to re-title an asset into your revocable trust, the Pour-Over Will is designed to receive those assets upon your death and “pour” them into your Revocable Trust. Second, the Pour-Over Will is the only place you can nominate a guardian for your minor children if you were to unexpectedly pass away. Finally, the Pour-Over Will distributes your personal property, such as your furniture, household items, clothing, etc. to your intended beneficiaries.

Martial Property Agreement

For married couples, we often draft a Marital Property Agreement. This agreement allows married couples to “opt in” to Wisconsin’s marital property system by classifying most of your assets as marital property upon yours and your spouse’s deaths. The Marital Property Agreement also contains a “Washington Will Provision,” which means the surviving spouse can fund the trust upon the death of the first spouse and thus avoid probate. This agreement, however, does not address divorce and is used solely for estate planning purposes.

Durable Power of Attorney

In the event that you become incapacitated as a result of an accident or illness, you can appoint an “agent” in your Durable Power of Attorney to oversee your financial affairs. We are often asked what the difference is between an “agent” and a “trustee.” An “agent” manages the assets outside of your Revocable Trust, while a “trustee” manages the assets held by your Trust. A Durable Power of Attorney offers great flexibility in administering your financial affairs and also allows you to avoid a costly guardianship proceeding.

Health Care Power of Attorney

A Health Care Power of Attorney allows you to appoint an individual to make health care decisions on your behalf in the event that you are unable to do so yourself. The document also allows you to express your wishes regarding entering a nursing home or community-based residential facility when the need arises, as well as other important end-of-life decisions.

HIPAA Release and Authorization

The Health Insurance Portability and Accountability Act was passed into law in 1996. This Act prevents medical professionals from divulging your personal medical records to family members or other individuals. Because of this, it is often difficult for family members to gain access to your medical information in the event of an emergency. Our HIPAA Release and Authorization allows medical professionals to release your personal medical records to persons of your choosing (often family members) to help manage your care.

Deed

If you establish a Revocable Trust, an important step is re-titling your real property into the name of your Revocable Trust. Thus, upon your death, you avoid having the real estate pass through probate, and your Trustee will have the ability to maintain, manage, and/or sell your real property upon your death. This step is especially important for property owned outside of Wisconsin. If you fail to transfer your real property into your Revocable Trust, you risk needing an "ancillary" probate in the state in which your real property is located. This can be a costly and tedious step we try to avoid.

TAX AND WEALTH ADVISOR ALERT: IRREVOCABLE INCOME-ONLY TRUSTS, HOW THEY CAN HELP YOU APPLY FOR MEDICAID AND WHEN THEY SHOULD BE AVOIDED.

An irrevocable income-only trust can be an indispensable tool when planning for retirement and long-term care expenses. It's important to know how these trusts work, how they help you qualify for Medicaid, and how to set one up.

What Are Irrevocable Income-Only Trusts?

Irrevocable income-only trusts are used for Medicaid planning. They are a type of living trust that protects assets from being sold to cover long-term care expenses such as nursing homes. These assets are placed in a trust so that they can be passed down to beneficiaries. The beneficiary of the trust is only entitled to receive the trust income; the trust principal is not accessible.

You can use an irrevocable income-only trust to qualify for Medicaid. You make your assets the trust principal, which becomes inaccessible to you. By doing so, you can only access the trust income, which is subsidized to pay for your nursing home care, and then Medicaid pays the rest. However, the amount Medicaid pays must be under $2,000 by the end of each month, and if not, it may increase the amount you pay out of pocket.

Qualifying for Medicaid

Although you can use this type of trust to help qualify for Medicaid, keep in mind, it creates a waiting period of ineligibility. Each state has laws about when you can start receiving

Medicaid benefits after transferring funds to an irrevocable income-only trust.

The Benefits and Downsides of Irrevocable Income-Only Trusts

An irrevocable income-only trust has several advantages, including:

- You retain the ability to qualify for Medicaid benefits and still preserve some assets for your loved ones.
- In the interim, between setting up an irrevocable income-only trust and entering a nursing home, you may establish an income stream for yourself.

There are some downsides to keep in mind when considering creating an irrevocable income-only trust, such as:

- You lose control over your assets in the trust. This is because the trust is irrevocable, which means you cannot change or terminate the trust.
- Medicaid's look-back period is 60 months, so if you become ill before this period ends, you are left without funds to pay for nursing home bills. Medicaid will not cover these costs. You should not put *all* of your assets in the trust for this reason.
- If you are young and healthy, a **revocable trust** is a much better structure for your estate plan because it allows you to change your estate plan and, more importantly, it keeps you in control of your assets.

How to Set Up an Irrevocable Income-Only Trust

To start an irrevocable income-only trust, you'll need to gather some important information. Make a list of your assets and income from all sources, including all assets transferred within the last five years. Then, determine whether your resources are exempt, non-exempt, or inaccessible for Medicaid purposes. Finally, consult with an experienced Medicaid law attorney to help you finalize and set up the fund.

Working with an experienced attorney can help you better ascertain your cash flow needs. You will have to ensure your present income needs are met and that you have sufficient funds to pay your nursing home bills if you unexpectedly become ill.

If you'd like further information about this topic, please contact a member of our Estate and Business Succession Planning team.

TAX AND WEALTH ADVISOR ALERT:

REMINDER—APRIL 18 IS THE DEADLINE FOR INDIVIDUAL RETURNS AND MORE

The filing deadline to submit 2021 tax returns or an extension to file and pay tax owed is Monday, April 18, 2022. By law, Washington, D.C., holidays impact tax deadlines for everyone in the same way federal holidays do. The due date is April 18, instead of April 15, because of the Emancipation Day holiday in the District of Columbia for everyone except taxpayers who live in Maine or Massachusetts. Taxpayers in Maine or Massachusetts have until April 19, 2022, to file their returns due to the Patriots' Day holiday in those states. Taxpayers requesting an extension will have until Monday, October 17, 2022, to file. Of note, the Monday, April 18 deadline is the deadline for more than just individual returns and extensions. Here is a list of some other April 18 deadline items that IRS has noted:

- Individual return extension requests. Taxpayers can extend the deadline beyond April 18, 2022, by filing Form 4868, *Application for Automatic Extension of Time To File U.S. Individual Income Tax Return.* Filing an extension moves the filing deadline from April 18, 2022, to October 15, 2022. You can also get an extension by paying all or part of your estimated income tax due with Direct Pay, the Electronic Federal Tax Payment System (EFTPS), or a credit or debit card.
- Contributions to IRAs and health savings accounts. Taxpayers only have until April 18, 2022, to make 2021 contributions to individual retirement arrangements (IRAs), Roth IRAs, health savings accounts, Archer medical savings accounts, and Coverdell education savings accounts—even if they file for an extension.
- Self-employed persons retirement plan contributions. Self-employed persons have the opportunity to fund SEP and SIMPLE IRAs as well as solo 401(k) plans through the deadline for a timely filed extension.
- Withdrawals of any 2021 contributions to an IRA. Withdrawals of any 2021 contributions to an IRA, including excess 2021 contributions (if you didn't request a filing extension), are due April 18, 2022. This rule also applies to the following retirement plans: 401(k), 403(b), SARSEP and SIMPLE IRA plans.
- Payroll taxes for household employees. Form 1040, Schedule H (Household Employment Taxes) is due even if you are not required to file Form 1040 itself.
- 2018 unclaimed refunds. The law provides a three-year window to claim a refund. To get any unclaimed refund from 2018, a taxpayer must properly address and mail the tax return, postmarked by April 18, 2022. If a taxpayer does not file a return within three years, the money becomes property of the U.S. Treasury.
- Returns for calendar year tax-exempt organizations. Also due April 18, 2022, are forms in the 990 series, including Form 990-T, *Exempt Organization Business Income Tax Return*.
- Foreign trusts and estates. Foreign trusts and estates with federal income tax filing or payment obligations that file Form 1040-NR also have until April 18, 2022, to file or make payment.
- State individual income tax returns for most states. Most states follow the federal due date. However, as mentioned above, taxpayers in Maine or Massachusetts have until

April 19, 2022, to file their returns due to the Patriots' Day holiday in those states. The filing due date for Wisconsin is April 18, 2022. Nevertheless, if you need more time to file, Wisconsin offers an extension. Wisconsin does not have its own separate extension application. If taxpayers have an approved federal tax extension (Form 4868), they will automatically receive a Wisconsin tax extension. Filing a federal extension moves the Wisconsin filing deadline from April 18, 2022, to October 15, 2022.

Timely and Accurate Mailing

The IRS encourages taxpayers to e-file their returns or extensions. If you are planning on filing a paper return, extension or even paying by check, be sure to put the return, extension and/or check in first-class mail by the due date. As long as your return is postmarked by the due date, the IRS considers your return or extension to be filed on time. In the event of a dispute, you need to prove that you mailed your tax return or extension on time. Stating that you mailed the return won't be enough proof without additional documentation. The best method is to send by registered mail which is confirmed by Section 7502(c) of the Tax Code.

It is also important for taxpayers to check that the any tax forms or payments are sent to the correct address. The correct address should be listed on the instructions to the form you are filing, but the IRS's website also provides a listing here. In addition to mailing through the U.S. Postal Office, certain private delivery services designated by the IRS can also be used. See the IRS's list here. Note that many private delivery services cannot deliver to a P.O. box, but you can find a list of addresses for private delivery services on the IRS's website.

For questions or further information relating to the tax filing deadlines, please contact Attorney **Britany E. Morrison**.

AN EDUCATIONAL BUSINESS SERIES FOR SUCCESS: SETTING IN PLACE AN EXIT STRATEGY WHEN THE TIME COMES AND MINIMIZING THE POTENTIAL FOR CONFLICT

In our last article, we reviewed why creating a buy-sell agreement can protect the owners of a company and help guide the process of a business succession plan. In this post, we will review how to create an exit strategy and minimize conflict when it comes time to begin to transfer the business.

PART 2 – SETTING IN PLACE AN EXIT STRATEGY WHEN THE TIME COMES AND MINIMIZING THE POTENTIAL FOR CONFLICT

Whether it's in personal relationships or business, the old song is right: "Breaking up is hard to do." Sure, you go into the company with starry eyes and big dreams, but you also must be a realist and know that things could go south quickly and unexpectedly — and splitting up can get ugly fast.

The best way to ensure a smooth transition when the time comes is to devise an exit strategy that will minimize the potential for conflict. A well-designed buy-sell agreement can act as your road map for how the business's owners will act and respond in the case of certain triggering events. Think of it as a prenuptial agreement but in the business world, and keep your focus on the goal of making the breakup go as smoothly as possible.

Although a buy-sell agreement makes it sound like someone is buying and selling a business, what it really does is sets out the circumstances under which the business's owners can sell their interests, who can purchase them, and the value of the interest. Let's take each of those aspects separately and delve deeper.

Triggering Event

When a business owner can sell his or her interest is generally called the "triggering event." Just as its name implies, the triggering event is what sets the buy-sell agreement in motion, and it generally occurs with the death, illness, disability, retirement, divorce, or bankruptcy or insolvency of an owner (partner or shareholder). Alternatively, an owner just may simply want out of the business for personal reasons, or you may want to terminate the employment of one of the business's owners within the company. A buy-sell agreement can cover any, some, or all of these events, depending on the preferences of the company's owners.

Who Can Purchase the Interest

One of the best parts about being involved in a closely held company is that its owners get to decide who their co-owners are – usually other stockholders. A solid buy-sell agreement maintains this owner freedom by specifying who may purchase an outgoing owner's interest in the business. For instance, the owners may agree that their spouses or children will always have first dibs on their ownership interests.

Valuation

The importance of placing a value on the ownership interest while in calm, non-volatile times cannot be overstated. When a triggering event occurs, emotions can run high, and depending upon the circumstances, so can animosities and other unflattering and unproductive feelings. In other words, this is not the time you want to be haggling over the price of an owner's

interest in the business. Leaving the price open until that point could result in different owners wanting to use different valuation formulas or disagreement on selecting a professional appraiser.

Accordingly, to avoid problems regarding valuation, the best course of action is to have it determined before any kind of triggering event and while everyone is still working collaboratively toward common goals. This value then gets memorialized in the buy-sell agreement, and once it must go into effect, owners don't have a lot of room to complain about it. However, since the value of a business will change annually, so should the value be updated annually. If such value has not been updated for 18 (or 24) months prior to the Triggering Event and is not covered by a formula which automatically updates the value, then the value should be obtained by an appraisal of the business by an appraiser qualified to handle such job.

Just as with a prenuptial agreement, a buy-sell agreement is tailored to fit your individual needs. Just like no two marriages are alike, your buy-sell agreement should not simply have boilerplate language either. While you may be able to find templates online, a buy-sell agreement should reflect the specific needs and circumstances of an individual business to avoid the risk of facing legal challenges later.

The main goal, after all, is always to put in place an agreement among business partners as to what the end of a relationship will look like and leave as little room as possible for conflict, especially in terms of litigation, the costs of which could hamper, or even destroy, what's left of your business. Besides, at the end of a relationship — business or personal — no one needs added stress, and that's exactly what a properly drafted buy-sell agreement can help eliminate.

Check out our next article in our business series explaining how ownership interests can be transferred if one or more of the owners can no longer or do not want to continue in the business.

If you have questions about your company's succession, please contact a member of our Estate and Business Succession Planning team.

Other articles in this series:

- An Educational Business Series for Success: Why Buy-Sell Agreements are Necessary Even if You Don't Plan to Sell Your Company Soon

AN EDUCATIONAL BUSINESS SERIES FOR SUCCESS: WHY BUY-SELL AGREEMENTS ARE NECESSARY EVEN IF YOU DON'T PLAN TO SELL YOUR COMPANY SOON

Long before a closely-held business is readied for sale, it should be protected by the owners creating a buy-sell agreement. In short, every co-owned business needs a buy-sell, or buy-out agreement the moment the business is formed or as soon after that as possible. A buy-sell, sometimes called a buy-out agreement, protects business owners when a co-owner wants to leave the company (and protects the owner who is leaving). It also contemplates dealing with unforeseeable catastrophic events, such as owner death or disability. We recommend business owners create a buy-sell agreement as soon as the business is formed because, as is often said: "It's a lot easier to get an agreement in place when everyone's in agreement."

We have broken down the key elements and thinking that go into a buy-sell agreement into a series for business owners to find success.

PART 1 – PROVIDING A MARKET FOR THE OWNERSHIP INTEREST OF THE CLOSELY-HELD BUSINESS UPON A SPECIFIED "TRIGGERING EVENT"

Being able to work with people you know and trust in a closely-held business can be an invaluable experience, but among the many practical advantages is that the partners hold a great deal of control over their own companies. With fewer government regulations restricting their actions and decisions, owners can choose what to do with their profits—pay themselves, donate to charity, reinvest, etc.—and they generally enjoy the freedom to try out new ideas and pursue higher risk, higher yield options that might not fall in line with a corporate shareholder's more conservative judgment.

That said, the many pluses of closely-held companies do come with some minuses, and one of those is the potential inability to sell the business or some of its ownership interests when necessary. That time may come for a variety of reasons, both unexpected and planned from death and illness to retirement, and the so-called "triggering event" can wreak havoc on the enterprise.

More on Triggering Events

Most commonly, a buy-sell agreement kicks in at the death of an owner and requires the surviving owners or the company to purchase the deceased owner's interest from their estate. Death isn't the only possibility of a triggering event, however. Any number of situations could arise that could send a business into disarray, including the following:

- Sudden illness, disability, or incapacitation
- Retirement
- Divorce
- Termination of the employment of the owner within the company
- Bankruptcy or insolvency of the owner in question
- Lack of desire of owner to continue in business

The reality is that without a buy-sell agreement in place, closely-held businesses run a high risk of not being able to be sold, either in whole or in part, when a triggering event happens. The best course of action to prepare for this scenario is to create a buy-sell agreement and provide a method for valuing the business within the agreement so you can avoid potentially catastrophic consequences to your business later.

The Importance of a Buy-Sell Agreement

Having an exit strategy in place, notably in the form of a buy-sell agreement, is an excellent way to help ensure your business doesn't go under when a triggering event occurs. A buy-sell agreement that has already been agreed to in advance, independent of emotions that could be heightened during challenging times, can help resolve matters quickly and in the best interests of the business.

Having a buy-sell agreement in place when emotions are running high is also beneficial for valuation purposes. Even if you can come to a reasonable, fair value, it can be even more challenging to get a potential buyer to agree with you on the acceptable sale price, especially depending upon the circumstances of the triggering event.

Valuing the business during the calm times provides not only an unbiased valuation, but also a market for the ownership interest in the enterprise upon a triggering event that is specified within the buy-sell agreement. Quite simply, having a buy-sell agreement in place ahead of time can mean the difference between a successful passing on of the business and its folding; the agreement can provide a market for what may be an otherwise unmarketable interest that no one would want or perhaps even be able to buy. While drafting a buy-sell agreement helps put a number to the value of each business owner's interest, it also makes sure that the remaining owners have complete say over who their next partner will be or even whether they want anyone else in the business at all. Moreover, with a buy-sell agreement in place, surviving or remaining owners are less likely to have grounds to pursue litigation—which can be expensive, time-consuming, and end up harming or even destroying the business.

Check out our next article in our business series covering what type of exit strategy needs to be considered in a transition.

If you have questions about your company's succession, please contact a member of our

Estate and Business Succession Planning team.

TAX AND WEALTH ADVISOR ALERT: WISCONSIN TO ALLOW MUNICIPALITIES TO WAIVE PROPERTY TAX PENALTIES AND EXTEND CONSTRUCTION AND BUILDING PERMITS

Wisconsin Governor Tony Evers has signed Senate Bill 254, which affects building permit holders and late property tax payments. The bill, which Evers signed on Friday, October 15, 2021, and is now known as 2021 Wisconsin Act 80, allows municipalities and other taxation districts to waive interest and penalties on late 2021 property tax payments. It also adds a timely payment requirement for filing certain property tax claims if payment was submitted by October 1, 2021. The Act also allows holders of certain unexpired construction or building permits or approvals to seek extension of the permit or approval term if the permit is subject to administrative, judicial, or appellate proceedings that may result in the invalidation, reconsideration, or modification of the permit or approval.

For questions or further information relating to 2021 Wisconsin Act 80, please contact Attorney Britany E. Morrison.