

Tax-Efficient Succession Plan **BUSINESS PLANNING**

A TAX-EFFICIENT PLAN TO KEEP THE PRACTICE TOGETHER

Professional partnerships often struggle with the issue of business succession. Whether it is a law firm, accounting firm, or a medical practice, senior partners often prefer to keep the practice together by transitioning ownership to junior partners, instead of selling to private equity buyers. However, junior partners may struggle to pay large lump-sum amounts to retiring partners or to qualify for bank financing at low rates. Tax-Efficient Succession Plans allow retiring partners to transition the business to the next generation in a way that amortizes the cost over many years. Additionally, the retiring partner may receive a significant after-tax premium to the current value of their interests.

HOW TAX-FREE MANAGEMENT BUYOUTS WORK

1. Practice borrows money from a bank to fund a cash value life insurance policy on Senior Partner.
2. Junior Partner(s) pay annual interest due on the bank loan.
3. After 7-10 years, Practice uses cash value to make partial repayment of bank loan (50-75%).
4. Practice refinances remaining loan as traditional acquisition loan, amortized over 10 years.
5. Practice distributes life insurance policy with substantial cash value to Senior Partner, in liquidation from the Partnership.



If structured correctly, and under current tax law, the distribution of a life insurance policy should not be a taxable event for income tax purposes. Clients must consult with their own legal and accounting professionals and should not rely on information contained herein as tax advice or consulting.

-SEE CASE STUDY ON NEXT PAGE-

TAX-EFFICIENT SUCCESSION PLANS WORK WELL FOR CLIENTS WHO:

- *Plan to retire in 7 to 10 years*
- *Prefer to keep ownership with junior partners*
- *Junior partners who cannot personally qualify for large bank loans*

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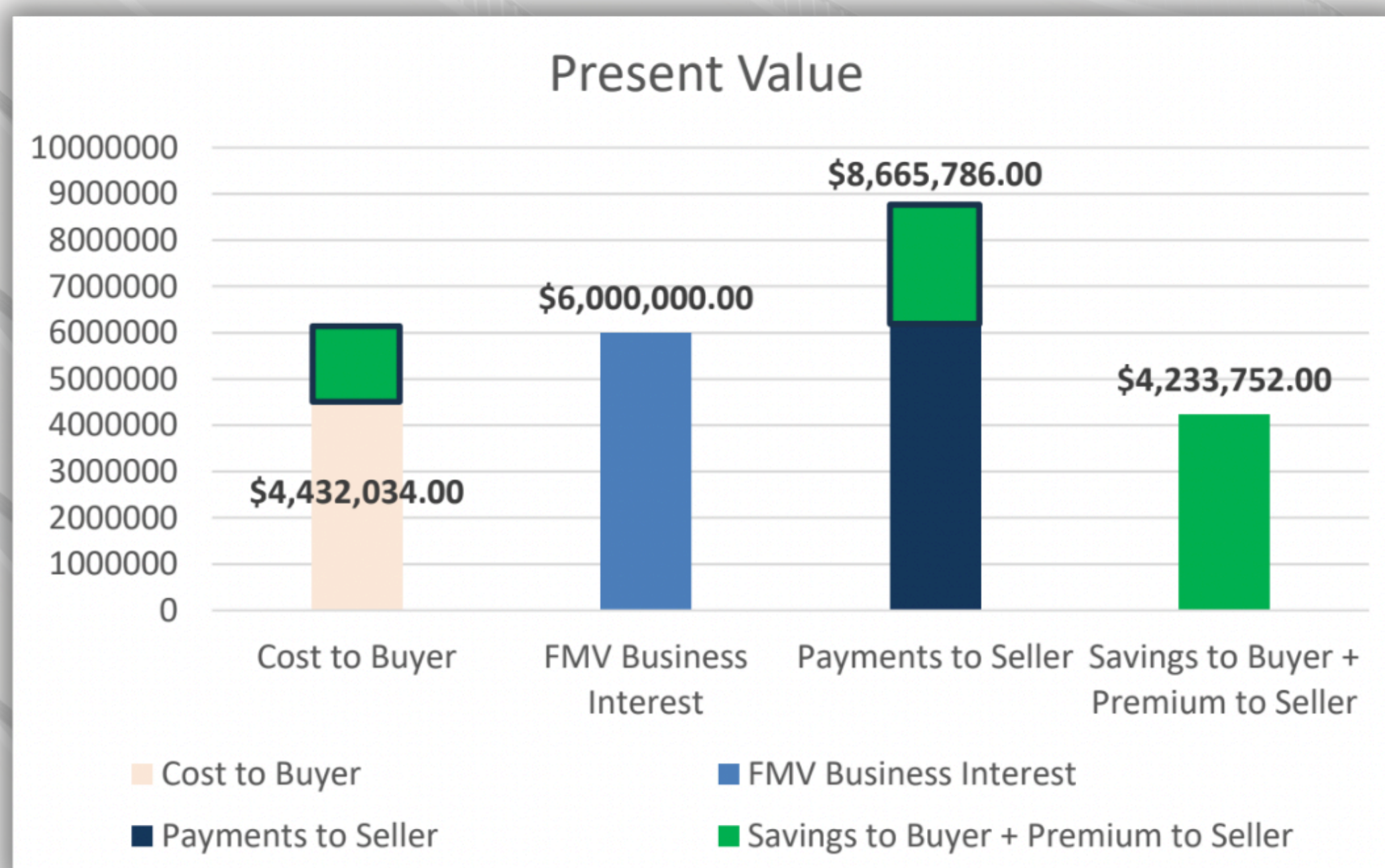
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CASE STUDY: DENTAL FACILITY IN NY

Sam is a Senior Doctor at a dental facility in New York. The Dental practice is estimated to be worth \$10M today, with Sam owning 60%. Sam is expecting to retire in about 10 years and is thinking about how to begin transitioning ownership to the next generation of doctors at the practice. The Junior doctors do not have significant earnings yet to qualify for bank financing or to allow for a large lump-sum payment or large installment payments. Instead, Sam arranges for a bank financed insurance policy, to be owned by the Practice, and to be paid for by the Junior doctors. Since the bank loan is funded over 10 years, the interest payments for the Junior doctors over the first 5 years are significantly more affordable. After all premiums have been funded the Practice can repay a significant portion of the bank loan from the cash value, and still have a large amount of net cash value in the policy. The Practice can then distribute the life insurance policy to Sam, who can continue to borrow against the cash value as a form of tax-exempt retirement income. **By amortizing the cost over 20 years, the Junior doctors will be able to acquire the practice at a significant discount to market value, and by using leverage and tax-exempt assets, Sam will sell his practice at a significant after-tax premium to market value.**



WHAT DETERMINES THE BENEFITS?

The benefits of Tax-Efficient Succession Plans are a function of many factors, including:

- *Time until retirement for the Senior Partners (the longer, the better)*
- *Current and future loan interest rates (the lower, the better)*
- *Current and future income tax rates (the higher the rate, the larger the value of the tax-exempt buyout)*

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