Strategic wealth management for entrepreneurs and business owners

Volume 2 | Growing a business
Who should be on the growth phase advisory team and what specific roles do they play in assisting a business owner?  pg. 6

Why is it important to coordinate one’s estate plan with the growth of one’s business?  pg. 10

How conducive is the current tax landscape toward estate and gift planning?  pg. 11

What types of trust structures provide strategic benefits to an entrepreneur whose business is in the growth phase of its strategic life cycle?  pg. 13

What are examples of typical business, personal and family priorities and how can compartmentalized planning undermine an entrepreneur’s ability to address them?  pg. 17

Why should a business owner develop an integrated wealth management plan that takes into account business, personal and family priorities?  pg. 26

What are the key “next steps” that a business owner should consider regarding subsequent phases of his or her company’s life cycle?  pg. 32
Contents

Introduction.............................................................................................................................................. 2

About this volume................................................................................................................................. 4

Step 1: Select a growth phase advisory team..................................................................................... 5
  The advisory team: Composition and roles..................................................................................... 7

Step 2: Review your trust and estate planning needs......................................................................... 9
  Current tax landscape for estate and gift planning........................................................................ 11
  Using trusts to benefit from a company’s anticipated appreciation in value.............................. 13
  Using a Family Limited Partnership.............................................................................................. 14

Step 3: Align business, personal and family priorities...................................................................... 15
  The risks associated with compartmentalized planning.............................................................. 16
  An integrated planning approach.............................................................................................. 18
  Understanding employee compensation plans.......................................................................... 21
  Balancing the interests of the owner and his/her children......................................................... 23

Step 4: Develop an integrated plan................................................................................................... 25
  An integrated wealth management plan in action....................................................................... 26

Step 5: Consider “next steps”........................................................................................................... 31
  Preparation for the post-growth phase......................................................................................... 32

Conclusion ............................................................................................................................................ 34
“Perpetual devotion to what a man calls his business is only to be sustained by perpetual neglect of many other things.”

Robert Louis Stevenson
“Perpetual devotion to what a man calls his business is only to be sustained by perpetual neglect of many other things.” – Robert Louis Stevenson

Perspective – growth versus development

For many business owners, the passion with which they pursue their dreams is matched only by the toll that the endeavor takes on other aspects of their lives. In this regard, many might argue that the concepts of entrepreneurialism and balance share only one thing – their mutual exclusivity. And yet, it need not be so – at least where strategic wealth planning is concerned.

Indeed, when carefully conceived, skillfully executed, and intelligently maintained, an integrated wealth plan can serve to align the interests of entrepreneurs, their businesses, and their families in ways that are both enduring and impactful.

This is essential, for there are few things as tragic as those entrepreneurs whose professional success comes at the expense of the very things that they hold most dear – their personal and familial fulfillment.

Challenge and opportunity – an alignment of interests

This publication – Strategic wealth management for entrepreneurs and business owners (Volume 2: Growing a business) – seeks to reinforce the notion that growing an entrepreneur’s business can be accomplished in tandem with pursuing family and personal wealth management priorities.

Holistic wealth management – the Barclays approach

At Barclays, we understand the aspirations that you have for yourself, your business and your family. We look forward to working with you to see those dreams realized.

Christopher Johnson

Head of Wealth Advisory and Strategic Solutions, Americas
Six-volume series: Strategic wealth management for entrepreneurs and business owners

Volume 1 | Forming a business
Volume 2 | Growing a business
Volume 3 | Transitioning the business to family members
Volume 4 | Pre-IPO planning
Volume 5 | Pre-Sale planning
Volume 6 | Post-Exit considerations

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About this volume

The “growth phase” of a company’s life cycle occurs immediately after its “formation phase” and serves as the period of organizational maturation and tactical alignment leading up to an eventual exit strategy. Generally speaking, there are three primary exit strategies:

> Transitioning the business to family members (e.g., children)
> Preparing for an initial public offering (“IPO”)
> Selling the business to a third party

Figure 1: Strategic life cycle of business ownership

Although each company will ultimately forge its own strategic path, there are specific steps that each entrepreneur should take when growing his or her business, including:

> Assembling a “growth phase” advisory team
> Reviewing trust and estate planning needs
> Aligning business, personal and family priorities
> Developing an integrated wealth management plan
> Considering next steps

Each of these elements will be addressed in turn.

1. For additional information regarding the “formation phase” of a company, see the first volume of this series – Strategic wealth management for entrepreneurs and business owners (Volume 1: Forming a business).
2. These three strategies are explored at length in volumes 3, 4 and 5 of this series – Strategic wealth management for entrepreneurs and business owners.
Step 1
Select a growth phase advisory team
A growth phase advisory team is a network of professional advisors whose individual and collective expertise can serve to provide business owners with the guidance and insight necessary to develop a sound wealth management plan.

Q: Who should be on the growth phase advisory team and what specific roles do they play in assisting a business owner?

The growth phase of an organization’s life cycle is normally the longest phase in terms of duration. During this period, the composition of a business owner’s advisory team is likely to vary depending upon the specific nature of the challenges and opportunities being addressed.
Although the specific configuration of the team will vary depending upon the circumstances, the advisory team of a business owner in the growth phase of his or her business will normally consist of some (or all) of the following advisors:

**The Certified Public Accountant (“CPA”)**
Accountants are among an entrepreneur’s most important advisors. Indeed, their extensive knowledge of a business owner’s tax, compliance and financial history make them an indispensable resource during the growth phase of a company’s life cycle.

**The Corporate Attorney**
As a company grows, it will normally require the services of a Corporate Attorney to assist in the oversight of various commercial, contractual and regulatory responsibilities.

**The Insurance Agents**
Ideally, a business owner will have acquired a range of insurance coverage from a licensed insurance agent during the formation phase of his or her company’s life cycle. This coverage will normally include elements of: (i) property and casualty insurance; (ii) directors and officers liability insurance; (iii) liability insurance for employees; (iv) errors and omissions insurance; and (v) life insurance. As the company grows in conjunction with an owner’s wealth profile, periodic insurance reviews should be undertaken in order to ensure that coverage remains adequate and appropriate.

**The Investment Banker**
Although Investment Bankers normally become more relevant to business owners in the period leading up to an IPO, merger or acquisition, business owners should work with their advisory team from an early stage to prime and position the company for those exit strategies (presumably, the ultimate goal).

**The Investment Representative (“IR”)**
At this stage in the business’s life cycle, an entrepreneur’s relationship with an Investment Representative will be partially dependent upon the amount (and nature) of the investable wealth that he or she possesses. However, even in instances where an IR is not directly assisting in an investment capacity, he or she can still serve a valuable role by offering support, guidance and introductions to other key players within the firm (e.g., Investment Bankers).

**Investors**
A growing business will often require additional capital to fuel its development. This can originate from a range of sources including banks, venture capital and private equity firms, etc.

**The Valuation Consultant**
An expert and impartial valuation of a business serves as a key planning component for several estate, tax and pre-exit strategies. These are best obtained through the utilization of an experienced Valuation Consultant.

**The Trustee**
Where individual Trustees are utilized in addition to (or as an alternative to) corporate trustees, care should be taken to select trustees who can serve in a fiduciary capacity without concern regarding objectivity, skill, or conflicts of interest.

**The Trust & Estate Attorney (“T&E Attorney”)**
An integrated estate plan that addresses an individual’s personal and commercial business interests is an essential component of any entrepreneur’s wealth management undertaking. A primary architect of such a plan should be an experienced Trust & Estate Attorney.

**The Wealth Advisor**
A Wealth Advisor, by virtue of his or her training in tax, trusts and estates, will normally collaborate with an Investment Representative (and other advisors) to help optimize a client’s wealth management plan.

Neither Barclays in the US nor its Wealth and Investment Management employees in the US render tax or legal advice. Please consult with your accountant, tax advisor, and/or attorney for advice concerning your particular circumstances.
Figure 2: Business owners should leverage a core advisory team to resolve key business issues

- Refine trust & estate structuring
- Trust & Estate Attorney
- Corporate Attorney
- Trustee
- Wealth Advisor
- Insurance Agent
- Investor
- Investment Banker
- Valuation Consultant
- Investment Representative
- Accountant
- Trust & Estate Attorney

Align business, personal and family priorities
Map out an integrated wealth planning process
Identify an exit strategy
Growth phase business owner
Step 2

Review your trust and estate planning needs
As a general rule, estate planning is most effective when undertaken early on within the life cycle of a business.

Early on in the life cycle of a business, company valuations tend to be lower and the time horizon remaining until an eventual “exit” from the company can allow an entrepreneur to engage in a broad range of impactful planning activities.

Figure 3: Building a comprehensive plan adds value at all stages of the development of a business

Q: Why is it important to coordinate one’s estate plan and the growth of one’s business?

The early stage of a company’s growth phase is often a particularly productive time for the owner(s) to conduct in-depth estate planning. Unfortunately, the demands associated with a growing business tend to be all-encompassing. As a result, business owners often fail to implement any type of estate plan until one is imposed upon them by virtue of an impending exit from the business or their own (untimely) passing.

For those entrepreneurs who do undertake thoughtful business and estate planning, the resultant rewards can include:

> A more efficient business transition (either via intra-familial transfer, IPO or sale)
> An increased likelihood of successfully achieving financial, commercial and familial goals
> A minimization of estate and gift taxes
Q: How conducive is the current tax landscape toward estate and gift planning?

Currently, the applicable federal legislation provides individuals with an unprecedented opportunity to engage in sophisticated wealth planning – one where the estate tax, gift tax and generation-skipping tax (GST) exemption thresholds each exceeds $5 million dollars.

Furthermore, the corresponding maximum federal tax rate is 40% (in those instances where the imposition of tax cannot be completely avoided).

By virtue of these liberal planning parameters, business owners who benefit from access to sophisticated estate and tax planning expertise can position themselves to distribute substantial wealth to subsequent generations (should they so desire) with little or no transfer tax consequences.

The chart below summarizes the historical federal estate, GST and gift tax exemptions.

**Figure 4: Historical estate, GST and gift exemption values and rates**

<table>
<thead>
<tr>
<th>Calendar year</th>
<th>Estate tax exemption</th>
<th>GST tax exemption</th>
<th>Gift tax exemption</th>
<th>Top estate, GST and gift tax rates</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>$1 million</td>
<td>$1.12 million</td>
<td>$1 million</td>
<td>49%</td>
</tr>
<tr>
<td>2004</td>
<td>$1.5 million</td>
<td>$1.5 million</td>
<td>$1 million</td>
<td>48%</td>
</tr>
<tr>
<td>2005</td>
<td>$1.5 million</td>
<td>$1.5 million</td>
<td>$1 million</td>
<td>47%</td>
</tr>
<tr>
<td>2006</td>
<td>$2 million</td>
<td>$2 million</td>
<td>$1 million</td>
<td>46%</td>
</tr>
<tr>
<td>2007 and 2008</td>
<td>$2 million</td>
<td>$2 million</td>
<td>$1 million</td>
<td>45%</td>
</tr>
<tr>
<td>2009</td>
<td>$3.5 million</td>
<td>$3.5 million</td>
<td>$1 million</td>
<td>45%</td>
</tr>
<tr>
<td>2010</td>
<td>(taxes repealed)</td>
<td>(taxes repealed)</td>
<td>$1 million</td>
<td>35% (gift tax)</td>
</tr>
<tr>
<td>2011</td>
<td>$5 million</td>
<td>$5 million</td>
<td>$5 million</td>
<td>35%</td>
</tr>
<tr>
<td>2012</td>
<td>$5.12 million</td>
<td>$5.12 million</td>
<td>$5.12 million</td>
<td>35%</td>
</tr>
<tr>
<td>2013</td>
<td>$5.25 million</td>
<td>$5.25 million</td>
<td>$5.25 million</td>
<td>40%</td>
</tr>
<tr>
<td>2014*</td>
<td>$5.34 million</td>
<td>$5.34 million</td>
<td>$5.34 million</td>
<td>40%</td>
</tr>
</tbody>
</table>

*Exemption figures will be inflation-adjusted in subsequent years.
Source Data: Internal Revenue Service (IRS) as of April 2014.

3. The GST exemption is the value that can be transferred to grandchildren and other remote descendants without additional (e.g., GST) transfer tax implications.
Q: How might trusts be used to assist a business owner with estate planning?

In light of the generous estate tax exemption amounts afforded by the passage of The American Taxpayer Relief Act of 2012, families will be able to pass significant wealth to their heirs without any tax planning. All families, however, must still account for the risks associated with leaving such wealth to beneficiaries in the absence of adequate protective measures. Those risks include lawsuits, divorce, future changes to the estate tax, and beneficiaries who are unprepared to inherit and manage such wealth.

There are a variety of structural approaches that individuals may wish to consider as they determine how best to move wealth to subsequent generations safely and efficiently. The most common solution involves establishing trusts for the benefit of family members and working with advisors to ensure that the terms of the documents reflect the grantor’s wishes. If properly structured, trust vehicles can prove to be an extremely effective means of accomplishing a family’s goals.  

The following figure highlights the basic workings and potential benefits of a trust.

Figure 5: Potential benefits of a trust structure

Consult with your Wealth Advisor and your Trust & Estate Attorney: Your Wealth Advisor and your Trust & Estate Attorney can provide guidance on appropriate trust structuring alternatives and can facilitate the structure’s incorporation into your broader wealth plan.

4. The results of an individual’s Financial Personality Assessment (“FPA”) can be extremely helpful in guiding one toward establishing the correct type of trust vehicle, as well as the best choice for trustee(s).
Q: How can trusts be used to benefit from the (anticipated) appreciation in a company’s value during its growth phase?

As the value of a company appreciates, it can become increasingly difficult to effectively redistribute the resultant wealth among family members. One solution to this dilemma involves establishing structures that permit beneficiaries to profit from the appreciation in company value while still minimizing the impact of estate and gift taxes.

Two planning structures that are commonly used in this regard are Grantor Retained Annuity Trusts (“GRATs”) and Intentionally Defective Grantor Trusts (“IDGTs”). Both approaches are especially popular with business owners, regardless of whether their ultimate exit strategy is expected to consist of:

- A transfer of the company to family members
- An Initial Public Offering (“IPO”)
- A sale of the company

In each case, the basic methodology associated with wealth planning consists of gifting ownership interests to beneficiaries while valuations are as low as possible. This approach removes the assets from the estate of the donor(s) and allows for much of the subsequent appreciation in value to accrue on behalf of beneficiaries.

The chart below compares and contrasts the salient characteristics of GRATs and IDGTs.

**Figure 6: Comparison of a GRAT to an IDGT**

<table>
<thead>
<tr>
<th>Description</th>
<th>GRAT</th>
<th>IDGT</th>
</tr>
</thead>
<tbody>
<tr>
<td>• An irrevocable trust (i.e., a trust neither revocable nor amenable by the grantor) designed to permit an individual to transfer the appreciation of assets in the GRAT with no gift tax consequence (through the use of annuity payments back to the grantor)</td>
<td>• An irrevocable trust designed to permit an individual to transfer the appreciation of assets in the IDGT with minimal gift tax consequences (through the use of a promissory note back to the grantor)</td>
<td></td>
</tr>
<tr>
<td>Advantages</td>
<td>• Effective for gifting highly appreciable pre-IPO stock to children or other beneficiaries</td>
<td>• Effective for gifts to grandchildren and other remote descendants</td>
</tr>
<tr>
<td>• Particularly useful for gifts of concentrated stock positions</td>
<td>• Short-term GRATs (i.e., &lt;10 years) are still permissible (but may be curtailed by future legislation)</td>
<td>• The interest rate charged by the grantor on the note is normally less than the rate used to discount the GRAT</td>
</tr>
<tr>
<td>• No gift tax exemption is used for zeroed-out GRATs</td>
<td>• Permits balloon payments on the promissory note (which can increase the effectiveness of the structure)</td>
<td>• The grantor can allocate GST to the IDGT</td>
</tr>
<tr>
<td>Disadvantages</td>
<td>• Benefits of a GRAT are often diminished when diversified assets are placed in the trust</td>
<td>• Benefits of an IDGT are often diminished when diversified assets are placed in the trust</td>
</tr>
<tr>
<td>• There is a mortality risk associated with a GRAT structure. If the grantor does not outlive the term of the trust, then the trust assets are not effectively removed from the estate</td>
<td>• Some gift tax exemption may be utilized with this structure</td>
<td>• May “waste” gift and GST tax exemption if assets do not appreciate</td>
</tr>
<tr>
<td>• The grantor cannot allocate GST during the primary GRAT term</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Notwithstanding the potential advantages of GRATs and IDGTs, consideration should be given to other issues involved in establishing the trust. Moreover, future changes in the law may affect planning. Neither Barclays in the US nor its Wealth and Investment Management employees in the US render tax or legal advice. Please consult with your accountant, tax advisor, and/or attorney for advice concerning your particular circumstances.
Consult with your Wealth Advisor and your Trust & Estate Attorney: Your Wealth Advisor and your Trust & Estate Attorney can educate you on the potential benefits of effectively utilizing GRATs or IDGTs in the overall context of your wealth and estate planning objectives.

Q: What is a Family Limited Partnership and how can it provide a planning benefit to entrepreneurs whose businesses are in the growth phase of their strategic life cycle?

A Family Limited Partnership (“FLP”) is a structure that allows individuals to gift limited partnership (“LP”) interests to family members or trusts while retaining a general partnership (“GP”) interest for themselves. As GPs, the individuals (in this case, business owners) maintain management and investment control over the FLP’s underlying assets as well as broad discretionary authority to determine the amount and timing of distributions.

The meaningful restrictions imposed upon limited partners (as well as their lack of control over the broader FLP structure) can provide substantial valuation discounts which, in turn, serve to minimize the impact of gift and estate taxes that the family might otherwise incur.

Figure 7: A Family Limited Partnership (FLP)

The figure above illustrates a sample FLP structure. In this example, the GP interests retain full oversight and control over the stewardship of the underlying business interests despite the fact that 99% of the “value” of that business interest has been conveyed to beneficiaries (e.g., children) through gifts of the LP interests.

Hypothetically, an entrepreneur might wish to convey a portion of the ownership interests in his or her business to the FLP during the growth phase of the company. The modest valuations of the (still) speculative business, in conjunction with the lack of control and lack of marketability discounts that may be offered by the FLP structure itself, can provide for a potentially effective means of wealth transfer.

Consult with your Wealth Advisor and your Trust & Estate Attorney: Your Wealth Advisor and your Trust & Estate Attorney can discuss the potential benefits and risks associated with incorporating FLPs into your wealth management strategy.
Step 3
Align business, personal and family priorities
Business owners often undertake their wealth management planning in a compartmentalized fashion. Although there are many possible reasons for this, a recurring theme arises with those entrepreneurs who are so focused upon the maintenance and growth of their businesses that all other considerations (i.e., personal and familial) take on a diminished relevance.

Even in those instances where personal or family priorities do receive equivalent attention, many entrepreneurs remain largely unaware of the potential benefits that can accrue when they embrace holistic wealth management methodologies.

Ultimately, however, the goal of any sound wealth management plan should be to acknowledge the interrelationship between all aspects of a business owner’s life. This can be achieved by adopting solutions that simultaneously address an entrepreneur’s:

- Business priorities
- Personal priorities
- Family priorities
Q: What are examples of typical business, personal and family priorities and how can compartmentalized planning undermine an entrepreneur’s ability to address them?

The figure below outlines some of the common questions that entrepreneurs focus upon when attempting to address the business challenges that may be of particular concern to them. Although each of these underlying topics constitutes a valid priority, the narrow manner in which each issue has been conceptualized may limit the ability of a business owner to engage in impactful wealth planning.

**Figure 8: Business priorities**

![Diagram of Business Priorities]

- How can I make the business more successful?
- How much should I pay my employees?
- How can I retain my employees?
- Do I wish to sell my business?

Similarly, in those instances where a business owner focuses his or her planning too narrowly upon personal considerations (such as retirement or liquidity), the resultant wealth management plan may undermine the interests of other relevant stakeholders (e.g., children or employees of the business).

The figure below highlights this mindset.

**Figure 9: Personal priorities**

![Diagram of Personal Priorities]

- Have I adequately prepared for my retirement?
- How much wealth should I exclude from my business?

There are also those occasions when the needs of entrepreneurs and their businesses are overshadowed by family priorities. Although some might consider the prioritization of one's family to be a noble gesture, any wealth management plan that aligns itself to a single facet of a business owner’s needs will almost invariably fail to deliver optimal results.
The figure below outlines some of the questions that might preoccupy an entrepreneur who adopts this perspective.

**Figure 10: Family priorities**

<table>
<thead>
<tr>
<th>Key priorities</th>
<th>Family priorities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business priorities</td>
<td>Family priorities</td>
</tr>
<tr>
<td>Personal priorities</td>
<td>Family priorities</td>
</tr>
</tbody>
</table>

- How can I provide for my family after I am gone?
- Are my children adequately prepared to deal with inherited wealth?
- Have I drafted an estate plan?
- Is my family situation stable?

**Q:** What is an alternative approach to addressing the underlying drivers of business, personal and family priorities?

By artificially segregating business, personal and family concerns, many entrepreneurs inadvertently undermine the wealth planning which is so crucial to them, their families and their companies.

Alternatively, entrepreneurs may wish to consider framing the solutions to the problems that they wish to attend to in holistic terms. Often, this will allow challenging problems to be addressed in a more logical, systematic and harmonious fashion.

**Figure 11: Holistic wealth management priorities**

- Do my exit plans for the business involve family succession?
- If so, how will I effectuate that transfer?
- If my exit plans do not involve succession, will my transition plans adequately provide for my retirement and the security of my family?
- Have I aligned my exit plan with my estate plan in order to ensure that my family is protected and provided for?

The figure above represents a modified approach to prioritizing wealth management needs – one that acknowledges their interrelationship at the most basic levels of analysis. Ultimately, although it is often convenient to analyze problems in a compartmentalized fashion, it is generally more productive to examine solutions to those problems in an integrated and holistic manner.

**Consult with your Wealth Advisor:** Your Wealth Advisor, in addition to your other advisors, can guide you through your business and estate planning process to help you achieve your holistic wealth management goals.
Q: What is a tangible planning example illustrating how personal priorities might effectively be addressed?

One of the most common (and potentially damaging) “personal priority” scenarios occurs in the case of a divorce. Beyond its obvious emotional impact, a bitterly contested divorce can curtail or even derail a growing company’s momentum.

Indeed, even the most amicable divorce can prove to be costly, time consuming and stressful – the challenge of which can be greatly complicated when a business serves as one of the couple’s primary assets.

Planning considerations:
In most instances, the need to divide marital assets will necessitate an independent valuation of the business. Following this, the couple must then determine whether to:

> Sell the business and divide the proceeds
> Continue to jointly operate the business following the divorce, or
> Allow one spouse to retain the business

Figure 12: Business options in the event of a divorce

Each of these options carries with it distinct strategic consequences.

Sell the business
Although selling the business and dividing the profits may appear, at first blush, to be the most straightforward solution, it should be noted that problems can arise if no suitable purchaser is on hand to acquire the enterprise.

Jointly operate the business
In some instances – often due to the difficulty associated with dividing a family-owned business – couples will attempt to continue to operate a business together following a divorce. Beyond the practical challenges of such an undertaking, the resultant stress placed upon employees, family members and the business itself can often result in this being the least desirable outcome for all parties involved.

One spouse retains the business
In cases where one spouse is more involved or attached to the business, it may make sense to have that individual “buy out” the remaining spouse’s interest or to provide him or her with other assets of equivalent value.
**Personal priority concerns:**
When analyzing the various strategic options available under such circumstances, a spouse’s visceral reaction may be to seek out the solution that addresses his or her personal priority – to pursue a path that is most subjectively beneficial – regardless of the potentially negative impact this approach may have upon other stakeholders. However, by taking the time to explore alternatives (with the assistance of external advisors), it may be possible to uncover a solution that is beneficial to all of those who have a vested interest in the company.

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**Hypothetical example***
Following 20 years of marriage, Bill and Mary decide to divorce. During that time, their widget-making business has prospered and is now worth $20 million dollars. Despite Mary’s desire to continue running the company, Bill’s initial thought is to seek a third-party buyer. However, neither spouse is keen to pay the resultant tax bill. After consulting with their advisory team, Bill and Mary decide to have Mary purchase Bill’s shares directly and continue operating the business on her own. Doing so, they are told, will allow the transaction to qualify as a tax-free “transfer of property incident to divorce”.

As a result, Bill will not have to pay capital gains on the increased value of the shares, as the transfer will not be characterized as a sale for tax purposes. Similarly, Mary will obtain a carryover basis in the stock (with capital gains being calculated when the stock is ultimately sold).

**Analysis**
This solution benefits Mary (who continues to run the company that she loves), Bill (who receives an optimal financial settlement), the company (which is buffered from the uncertainty associated with the protracted divorce proceedings which might otherwise have ensued), and Bill and Mary’s children (for whom the financial and emotional toll has been minimized).

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**Q:** What is a tangible planning example illustrating how business priorities might effectively be addressed?

One of the key areas of potential friction between employers and employees – especially in a growing business – stems from the issue of compensation. In the realm of entrepreneurship, it is often essential that the owner deploy a remuneration strategy that effectively aligns the growth and success of the business with the financial rewards that accrue to its employees.

The following chart highlights a range of alternatives in this regard while comparing and contrasting key elements of each approach, including:

- Restricted Stock (“RS”)
- Stock Options (Incentive Stock Options [“ISOs”] and Non-Qualified Stock Options [“NQOs”])
- Phantom Stock
- Stock Appreciation Rights (“SARs”)

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5. See IRC Sec. 1041.

*This hypothetical example is for informational purposes only. Future evidence and actual results could differ materially from those set forth in, or contemplated by, underlying statements. In light of these risks and uncertainties, there can be no assurance that these statements are, nor will prove to be, accurate or complete in any way.
Figure 13: Summary of employee compensation plans

<table>
<thead>
<tr>
<th>Elements</th>
<th>Restricted Stock (RS)</th>
<th>Employee Stock Options (ESO)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overview of plan</td>
<td>Restricted Stock is used for employee compensation. Usually RS vests after a number of requirements are met. At this point the stock becomes transferable.</td>
<td>Employee stock options may take the form of an ISO or an NQO. An ISO plan provides greater tax benefits to the employee but has more plan requirements than an NQO.</td>
</tr>
<tr>
<td>Prevalence of plan</td>
<td>Restricted stock plans are common ownership sharing plans (along with stock options) used by emerging businesses.</td>
<td>ESO plans are very common. Some emerging businesses shift from RS to ESO plans over time (to reduce the expense effect on the business).</td>
</tr>
<tr>
<td>Plan methodology</td>
<td>Plan-specific requirements (time or performance based) must be met between the receipt of the stock and the time when the stock vests (i.e., when stock is owned outright by employees).</td>
<td>ISO and NQO plans allow employees to buy stock at a specific value (for a period of time) and to exercise options at a later date (ideally at a significantly appreciated price).</td>
</tr>
<tr>
<td>Timing and ownership restrictions</td>
<td>Plans require a period of time to pass before stock can be fully owned by employees (or transferred as a gift – provided that a plan allows for this).</td>
<td>The plan period is measured from the purchase date until the date of exercise (sale). With an ESO plan, the employee can determine when to exercise the options.</td>
</tr>
<tr>
<td>Administrative duties</td>
<td>It is relatively easy for employers to track restricted stock grants and vesting periods, which makes this type of plan attractive for an employer to offer.</td>
<td>Some tracking is required in order for ESO plans to monitor pricing, awards and options exercise. Usually a software system is used for this purpose.</td>
</tr>
<tr>
<td>Employee taxation</td>
<td>Employees with a restricted stock plan do not incur an income tax liability until the stock vests.</td>
<td>Upon exercise, an ISO incurs no regular income tax (AMT may apply). Long-term capital gains will normally apply upon sale. An NQO plan incurs a regular income tax liability upon exercise.</td>
</tr>
<tr>
<td>Employer impact</td>
<td>Restricted stock requires employers to incur an annual expense over the term of the plan.</td>
<td>Employers generally prefer an NQO plan versus an ISO plan, as an income tax deduction can be taken upon NQO exercise. (No deduction can be taken with an ISO.)</td>
</tr>
</tbody>
</table>

Hypothetical example*

Fred has established a successful tech company. His long-term goal is to sell the business to a third party on favorable terms. Although his business has been growing steadily for the past three years, he feels that he has reached an inflection point that will require that he improve his profit margins if the business is to achieve the level of success that he believes it is capable of. His first thought is to implement a salary freeze within the organization. However, he is concerned that this may reduce productivity and limit his ability to hire (or retain) talented employees.

*This hypothetical example is for informational purposes only. Future evidence and actual results could differ materially from those set forth in, or contemplated by, underlying statements. In light of these risks and uncertainties, there can be no assurance that these statements are, nor will prove to be, accurate or complete in any way.
**Phantom Stock**

In phantom stock plans, the company pays cash (based upon the value of the ‘phantom’ shares) at a future date.

This is a less common ownership sharing plan as it entails more cumbersome administrative requirements for managing the plan.

Plans provide employees with a simulated stock issuance. As it is ‘phantom’ in nature, employees do not benefit from legal rights as ‘actual’ shareholders.

Stock is held from a grant date to a trigger date selected by employer (e.g., retirement). Employee is paid stock or cash based upon the amount of appreciation over the period.

Phantom stock awards are more cumbersome to track (versus other types of plans). Due to significant bookkeeping requirements, many employers opt not to offer phantom stock.

Employees cannot benefit from long-term capital gains treatment. Compensation is received as a future lump sum (a form of deferred compensation).

Phantom stock requires employers to report an ongoing liability and expense on financial statements (similar to any other form of deferred compensation).

**Stock Appreciation Rights (SARs)**

Stock Appreciation Rights are a form of ‘bonus’ compensation that do not require any stock purchase on the part of the employee.

SARs are less common. This type of plan is a blend of phantom stock plans and stock option plans.

SARs provide compensation to employees based upon the appreciation in stock value. The exercise date is left to the discretion of employees (not employers).

The plan period is measured from grant date until the date of exercise. Employees can determine when to exercise or trigger payment (the plan does not predetermine this).

Administrative duties with regard to SAR plans are very similar to those of phantom stock plans.

Employees cannot benefit from long-term capital gains treatment. Compensation is received as a future lump sum (a form of deferred compensation).

Employers benefit from a deduction, which is valued at the amount of income paid to employees for all SAR plans.

**Analysis**

Following a discussion with his advisors, Fred decides to implement a non-qualified stock option plan. The plan allows him to align the strategic vision of the firm with that of his employees. As a result, employee morale improves dramatically, providing the foundation for an increase in productivity and profitability, and ultimately makes the company a more appealing acquisition prospect.
Q: What is a tangible planning example illustrating how family priorities might effectively be addressed?

One of the most common tensions that exists within the context of estate planning stems from the question of how to balance the desire to redistribute wealth to beneficiaries (e.g., children) while not functionally impoverishing oneself.

This planning priority is especially relevant for the owners of businesses which are in the “growth phase” of their life cycles as these entrepreneurs must often align seemingly juxtaposed interests including:

> The desire to transfer wealth in a timely manner (i.e., before the rapidly increasing value of the business renders estate planning functionally ineffective)
> The unwillingness to divest themselves completely of control over income-producing assets (the access to which may become necessary to fund future business, personal or family needs)

Hypothetical example*

Tom and Alice own a successful and rapidly growing commercial real estate company. The pace of the company’s expansion is a mixed blessing, however, as they are concerned that the resultant size and illiquidity of their estate could render certain types of wealth planning impractical in the longer term. Further, having experienced the volatility of the commercial real estate market during the two decades that they have been in business, they are acutely aware of how quickly their fortunes can reverse upon themselves. Accordingly, they want any estate planning that they do undertake to acknowledge that uncertainty.

Analysis

In conjunction with their advisors, Tom and Alice decide to establish two Spousal Lifetime Access Trusts (“SLATs”), to be funded with portions of their real estate interests. The first SLAT will serve as an irrevocable trust that will be established by Tom for the benefit of Alice. In this case, Alice will be granted a “life estate” with the remainder interest passing to the couple’s children (and more remote descendants) upon her passing.

In conjunction with that undertaking, Alice will establish a second SLAT for the benefit of Tom and their children along similar lines. 6 This approach will allow the couple to move a significant portion of their wealth out of their estate while also permitting Tom and Alice access to the income generated by the underlying trust assets (should such access become necessary). 7

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6. In order to minimize the potential application of the reciprocal trust doctrine, many advisors would recommend that steps be undertaken to increase the “asymmetry” of the two trusts. There are different ways in which this may be accomplished including: (i) ensuring that each trust incorporates different co-trustees; (ii) ensuring that the trusts are not funded simultaneously; (iii) ensuring that the assets used to fund the respective trusts differ to a reasonable degree; and (iv) using different distribution standards in each trust.

7. As noted, there are numerous issues that would need to be considered when establishing such a structure – chief among them being the potential application of IRC Sec. 2036. In the event that SLATs were established for the husband and wife, respectively, care would have to be taken to avoid the possible ambit of the “reciprocal trust doctrine.” (See footnote (vi) supra, for discussion).

*This hypothetical example is for informational purposes only. Future evidence and actual results could differ materially from those set forth in, or contemplated by, underlying statements. In light of these risks and uncertainties, there can be no assurance that these statements are, nor will prove to be, accurate or complete in any way.
The figure below provides an overview of a hypothetical SLAT structure.

**Figure 14: A Spousal Lifetime Access Trust**

A trust is set up by each spouse for the benefit of the other spouse and ultimately their children.

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**Consult with your Wealth Advisor and your Trust & Estate Attorney:** Your Wealth Advisor and your Trust & Estate Attorney can educate you on the potential benefits of effectively utilizing SLATs as part of your wealth management strategy.

**Q:** What should entrepreneurs do once they have identified their primary business, personal and family concerns insofar as they relate to holistic wealth management?

After having identified the various drivers of their primary business, personal and family concerns, entrepreneurs should work with their advisors to craft an *integrated wealth management plan* that addresses each of these considerations. This planning should take into account the company’s near- and long-term strategic trajectory.

The following section of this document outlines this approach.
Step 4
Develop an integrated plan
After having identified the various drivers of their primary business, personal and family concerns, entrepreneurs should work with their advisors to craft an integrated wealth management plan that addresses each of these considerations. This planning should take into account the company’s near- and long-term strategic trajectory.

Q: What is meant by the term “integrated wealth management plan”?

An integrated wealth management plan charts the strategic path of an entrepreneur’s personal, business and family interests in a holistic fashion. It is designed to account for each inflection point in a company’s strategic life cycle and provides a means to engage in opportunistic planning in anticipation of those milestones.

Ideally, an integrated wealth management planning process also benefits from the input of the entrepreneur’s key advisors and reflects the various strategic facets of the business owner’s wealth management needs.

Q: What is an example of an integrated wealth management plan?

Consider the case of Rob and Rachel.

Case study facts:
- Clients: Rob and Rachel
- Children: 2 – Jake (20 years of age), Beth (18 years of age)
- Business: Manufacturing company
The “formation phase” strategy
In this illustration, Rob and Rachel meet with their Wealth Advisor to discuss how best to establish the foundation for their wealth management plan. They are preparing to launch their business venture and want to ensure that they are proceeding in a logical and appropriate fashion. Utilizing the information provided, the Wealth Advisor outlines a wealth strategy that addresses the couple’s key needs and concerns at each stage of their entrepreneurial life cycle.\(^8\)

It is uncommon for individuals to have the opportunity to develop an integrated wealth management plan during the \textit{formation phase} of their companies. Instead, they will normally engage in their first holistic wealth management discussion during the \textit{growth}, \textit{exit} or even \textit{post-exit} stage of their entrepreneurial life cycle.

In this case, however, Rob and Rachel are \textit{serial} entrepreneurs. Having previously launched and sold a company, they are aware of the benefits that can accrue from holistic wealth management and have sought to strategically align their planning accordingly.

Q: How would one develop an integrated wealth management plan that takes into account the formation phase of a company’s life cycle as well as the resultant business, personal and family priorities?

During the formative days of their company’s launch, Rob and Rachel work with their Wealth Advisor (and other advisors) to address their business, family and personal concerns in a holistic and integrated fashion, as shown in Figure 15. Ultimately, their accountant recommends that a C-Corporation (“C-Corp”) be established to house the company. During their discussion, it becomes clear that Rob and Rachel ultimately wish to exit the business via an IPO. They also stress the value of philanthropy as it relates to them (and their community).

\(^8\) Although this case study highlights an instance where an integrated wealth management plan is conceived during the “formation phase” of the business’ life cycle, such planning can obviously be undertaken at any point in time. However, there are key reasons why the “growth phase” of a company’s existence often serves as the ideal launching point for such an endeavor. Although the “formation phase” arguably provides the greatest opportunity for long-term planning, entrepreneurs may not have yet formulated the long-term strategies for the organization at this time. This can render integrated planning somewhat premature when embarked upon at the inception point of a business. By contrast, waiting until the business has had the opportunity to mature and develop a strategic vector can ensure that “integrated plans” more accurately reflect the opportunities and challenges that merit an entrepreneur’s consideration. Many business owners refrain from establishing a coordinated wealth management plan until the days or weeks prior to the crystallization of their exit strategy (e.g., through IPO, sale or transfer of the business). Although the planning that takes place at this time may still be effective, any actions that are undertaken earlier in the life cycle of the business (e.g., during the “growth phase”) will usually prove to be more effective and impactful (due to, for example, the impact of increased business valuations as the exit date approaches). The “growth phase” of a company’s life cycle can span years (if not decades). For this reason, it will normally provide entrepreneurs with the largest window for opportunistic planning by sheer virtue of its duration.
With these basic parameters in place, their Wealth Advisor begins to guide them throughout their long-term wealth management planning process.

The “growth phase” strategy

Having reviewed the pertinent elements of the integrated strategy as they relate to the company’s formation phase, the Wealth Advisor outlines the challenges and opportunities normally associated with the growth phase of an entrepreneurial endeavor.

Rob and Rachel have noted that intra-familial wealth transfer is a priority to them. In response to this, the Wealth Advisor provides guidance on several planning alternatives that may help enable them to distribute the wealth that may potentially accrue from the anticipated IPO in a tax-efficient and structured manner, as shown in the figure below.

![Figure 16: Stage 2 – “Growth phase” strategy](image-url)
For example, in order to minimize the gift and estate taxes associated with gifting transactions, shares of the C-Corp will be placed in a Grantor Retained Annuity Trust (“GRAT”). This will allow the couple’s children to participate in the increase in the company’s share value up to, and following, the IPO. Further, implementing the GRAT structure at this point in the life cycle of the organization ensures that valuations are as low as possible (thereby potentially increasing the efficiency of the structure).

To ensure that the children’s interests are protected, the proceeds stemming from the GRAT are channeled into carefully drafted trusts. In conjunction with this undertaking, the couple will embark upon a thorough review of their insurance and broader estate plan to reinforce an alignment of goals and priorities.

Finally, although the company will still be in its growth phase at this point in time, arrangements are made to have the couple’s Investment Representative provide introductions to a Barclays Investment Banking Team at the appropriate juncture. These preparations ensure that Rob and Rachel will be well positioned to embark upon their anticipated IPO exit strategy.

The “exit phase” strategy
In providing an overview of the anticipated exit phase of the company, the Wealth Advisor offers guidance in consideration of this next phase and its potential impact on the IPO. In light of business, personal and familial priorities, the couple is provided with an integrated IPO strategy that highlights the various steps that may be contemplated, in an effort to optimize their wealth management plan.

**Figure 17: Stage 3 – “Exit phase” strategy**

A key component of the strategy calls for consideration of a 10b5-1 plan. This will provide for the orderly sale of post-IPO stock in accordance with SEC regulations and guidelines. In conjunction with this, the increased value of the company stock may necessitate the utilization of a corporate trustee for the purposes of continuity and expertise of oversight. In order to facilitate this possibility, the Wealth Advisor ensures that the current trust documentation maintains the flexibility required to eventually utilize a corporate trust company.
The “post-exit phase” strategy
The outline for the post-exit phase of the plan is developed after speaking to Rob and Rachel about what issues may be relevant for them after they have transitioned away from the oversight of their company. Obviously, many of the specific details of the plan will be driven by variables that have yet to be determined (e.g., the timing of the IPO, the amount of wealth generated by the event, etc.). Despite this, the couple re-acknowledges that they would look forward to engaging in philanthropic activities following their exit from the business.

Figure 18: Stage 4 – “Post-exit phase” strategy

<table>
<thead>
<tr>
<th>Structure</th>
<th>Priorities</th>
<th>Reference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wife</td>
<td>Business Consider starting another business with children</td>
<td>Volume 1</td>
</tr>
<tr>
<td>Husband</td>
<td>Family Philanthropy Share values with children</td>
<td>Volume 6</td>
</tr>
<tr>
<td>Private Foundation</td>
<td>Personal Preserve wealth</td>
<td>Volume 6</td>
</tr>
<tr>
<td>C1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>C2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Children’s Trust</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Corporate Trustee</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

For illustrative purposes only.
Note: C1/C2 represent each of the two children with a beneficial interest in the Children’s Trust.

Having previously discussed Rob and Rachel’s charitable intent, the Wealth Advisor presents several philanthropic options. Ultimately, given the couple’s anticipated wealth profile, a private foundation is deemed to be the most feasible structure.

Utilizing a private foundation will permit Rob and Rachel to undertake a broad array of impactful charitable activities while also providing a mechanism for reinforcing family bonds (as their children will take an active role in overseeing the foundation and will assist in selecting the charities that will benefit from the endeavor).

Similarly, Rob and Rachel express the desire to potentially start yet another business at some point in the future. As these plans are discussed, it is noted that the couple’s children will be old enough at this point in time to actively participate in a joint entrepreneurial undertaking with their parents (a strategy which, in turn, provides yet another opportunity for Rob and Rachel to benefit their children by providing capital, expertise and guidance for the venture).

Finally, in order to address the desire to preserve and grow the wealth that was derived from the IPO, the couple will work with their Investment Representative to craft a bespoke investment portfolio that takes into account their unique mindsets, goals and investment needs.

Consult with your Wealth Advisor: Your Wealth Advisor, together with your Investment Representative and other advisors, can work with you and your family throughout your business and estate planning process to help you achieve your holistic wealth management goals.
Step 5
Consider “next steps”
Q: What are the key “next steps” that a business owner should consider at this juncture?

In many cases, the growth phase of the strategic life cycle of business ownership is characterized by a convergence of business, personal and family challenges. Despite this, an entrepreneur can capitalize on the maturation of his or her business endeavor by adopting a structured approach to wealth management – one that consists of:

> Assembling a “business growth” advisory team
> Analyzing applicable trust and estate plans
> Aligning business, personal and family priorities
> Developing an integrated wealth management plan

Although the growth phase of an entity’s life cycle can span years or even decades, an entrepreneur must nonetheless use this time period to carefully lay out the foundation for the next phase: an eventual exit strategy. Those business owners who proactively embrace this structuring methodology will find themselves well positioned to embark upon the subsequent stage of entrepreneurial planning – transitioning the enterprise.

In this regard, the three most common exit strategies include:

> Transitioning the business to family members
> Exiting via an Initial Public Offering (“IPO”)
> Selling the business

Consult with your Investment Representative: For an introduction into the planning considerations discussed above, ask your Investment Representative(s) for other volumes in the Series: Strategic wealth management for entrepreneurs and business owners.
“Only in growth, reform and change, paradoxically enough, is true security to be found.”

Anne Morrow Lindbergh
Conclusion

Incremental excellence

Anne Morrow Lindbergh once noted that, “Only in growth, reform and change, paradoxically enough, is true security to be found.”

For entrepreneurs seeking the security of an effective wealth management plan, salvation may ultimately rest upon three key endeavors: the alignment of their business’ “growth” strategies with their broader wealth planning, the reformation of their trust and estate documents to incorporate the strategies available to them, and a change in mindset that embraces holistic and integrated planning methodologies.

A shared vision

This publication seeks to assist business owners in developing customized solutions that address their highly individualized needs and goals. Ultimately, wealth management is a journey best undertaken with companions who understand the lay of the land and who come equipped with the tools necessary to traverse it.

At Barclays, we realize how challenging the passage from entrepreneur to investor can be, and we seek to collaborate with business owners in a manner that allows them to achieve their goals in the right way.

We look forward to being a source of guidance for you as you grow your business.
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