SPLITTING THE BUSINESS WITHOUT SPLITTING THE FAMILY

Estate Equalization

Life Insurance

PRUDENTIAL ADVANCED MARKETS TEAM
EXPERIENCED GUIDANCE FOR COMPLEX CHALLENGES

THE PRUDENTIAL INSURANCE COMPANY OF AMERICA

Prudential
Bring Your Challenges®

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HOW PRUDENTIAL CAN HELP

The Prudential Insurance Company of America and its affiliates offer a wide range of insurance products that can help your business continue successfully in the event of your death. Insurance is a vitally important business tool that is often overlooked.

Whether your business is a sole proprietorship, a partnership, a limited liability company, or a closely held corporation, Prudential can help. Purchasing insurance for business needs may prove to be one of the most important decisions of your life.

You've Built a Successful Business

Because you have worked so hard and put so much time and effort into your business, you want it to continue even after you are gone. Then you realize that there is another challenge that is perhaps as great as any you faced in establishing and growing the business.

That challenge is how to pass it to the next generation.

The liquidity and potential tax issues that you must resolve are difficult enough, but your situation is even more complicated because some of your children are directly involved in the business and others are not. You wish to treat all of your children equally, or at least fairly, but how can you do that if the business makes up the greatest portion of your estate?

The challenge

Equalizing the inheritance of the heirs.

In many family-owned businesses, the commitment and contributions the children make are not equal. Some children may work longer in the business than other siblings, often based on age, and feel they have a greater stake. Other children may choose not to join the family business at all to pursue other careers. One thing all the siblings have in common: they'll all want their fair share of the business when the time comes.

As a parent, you want to do the right thing, and often that means dividing what you have equally among your children.

That might seem fair, but for children who have been working in the business, the equal division of the business isn't fair. Unfortunately, it is not unusual that issues like this break families apart.

Let's look at a common family business situation.

Bob owns a successful business. He is married and has two children. While his wife, Susan, has been instrumental in the success of the business, she does not want to be dependent on it as her primary source of income after Bob's death. Their older son, George, shares his father's love for the business, but the younger son, John, does not and has chosen another career path. Bob's and Susan's goals are to:

- Ensure Susan will be financially secure.
- Leave the business to George.
- Make the inheritances of the two sons equal.

Eventually, the issues will be the same regardless of the order of the spouses' deaths. **If Bob is the first to die** and leaves Susan the use of all of their assets, Susan would have a business that she does not want, and George would not own a business that he *does* want.

The issue of equalization comes to the forefront at Susan's death. If Susan leaves the business to George, there will not be sufficient assets to equalize John's inheritance. If she divides the estate equally between them, George will have a partner who is not interested in the business and who will likely be a detriment to its continued success.

Taxes and other costs. To complicate the matter further, once the estate passes to children and not to a spouse, it may be subject to estate tax.* Plus there are settlement costs. So the question becomes from which share will the expenses be paid? If these expenses are paid from the business, there likely would be no business. If they are paid from non-business assets, John would end up with little or no portion of the estate. And dividing the burden equally between the two of them—which is the likely event—could cause the cessation of the business, and the liquidation of the securities and possibly the home.

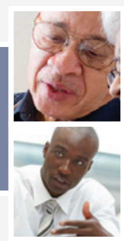
A solution

The wise use of life insurance.

The solution may lie in using life insurance and deciding when the family wants to equalize the inheritance. In the example family's situation, the desire is to pass the business to George at the death of his father and to make the inheritance to each son equal. Life insurance can be used to help achieve these goals.

An example of how using life insurance can help equalize the estate:

BOB AND GEORGE ENTER INTO A BUY-SELL AGREEMENT



1 A buy-sell agreement funded with enough life insurance can enable him to purchase the business from his father's estate.

LIFE INSURANCE

AT BOB'S DEATH THE INSURANCE PROCEEDS:

ENABLE GEORGE TO PURCHASE THE BUSINESS.

EQUALIZE THE INHERITANCE WITH JOHN.

2 At Bob's death, George uses the life insurance proceeds to purchase the business from Bob's estate. George then owns the business. The estate has cash to help equalize the inheritance to John.

If there is a concern that this will not leave Susan with enough assets, either John's inheritance could be deferred to the second death or additional life insurance can be acquired to provide for Susan.

Each family may have a preference of when to equalize inheritances.

In some cases, the desire is to have the children inherit after the deaths of both parents. In such a case, a child and his or her parents could enter into a buy-sell agreement funded with enough survivorship life insurance to enable the child to purchase the business at the death of the last parent to die. The assets remaining could then be divided equally among the children.

*The American Taxpayer Relief Act of 2012 (ATRA) makes permanent the $5 million exemption amounts (indexed for inflation) for the estate tax, the gift tax, and the generation-skipping transfer tax. In 2016 the exemption is $5.45 million, ($10.9 million for a married couple). The top tax rate, however, is increased to 40% (up from 35%) beginning in 2013. The Act also permanently extends the "portability" provision in effect for 2011 and 2012 that allows the executor of a deceased individual's estate to transfer any unused exemption amount to the individual's surviving spouse.

How do you know if estate equalization is right for you?

Estate planning concepts are never one-size-fits-all. Each situation requires a unique solution.

If you are a business owner, the solution presented in this brochure might be appropriate for you if your answers to the following questions are "Yes":

- Does your business account for more than half of your net worth?
- Would you like your business to remain in the family, managed by family members?
- Are family members currently active in the business?
- Do you have other family members who are not involved in the business? And do you want them to share in your estate?
- Do the active family members have the management experience necessary to succeed?
- Is it your intent to have your heirs inherit equal shares of your estate?
- Would you like another source of funds, other than the business, to provide for your spouse or heirs who are not active in the business?

CONCLUSION

The interplay of family, financial, and business concerns in estate and business planning can seem daunting, but it need not be. Equalization, as described, is quite simple conceptually, but there are issues that require assistance from a team of financial professionals that includes the insurance professional, an attorney, and a CPA. A talented and skillful team of professionals can help address and resolve—in an efficient and satisfactory manner—issues that may seem difficult at first.

THE PROTECTION COMPANY FOR OVER 140 YEARS

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