

Business & Estate Advisers, Inc.
With Your Interest In Mind

CASE OF THE QUARTER
CASE # 1
THE OLDER AND YOUNGER DENTISTS
(Or Lawyers, or Accountants, or Veterinarians, or Funeral Directors)

GOAL

To transfer the business from the older to the younger during the next ten years while securing a future for the exiting Dentist.

FACTS

Older Dentist is 55 and younger one is 30. There are four other employees. Practice is worth \$400,000. Current retirement plan contribution is \$40,000 per year with \$20,000 going to older Dentist and \$5,000 to younger Dentist. Practice income exceeds older Dentist current needs so would actually like to save more in the retirement plan. Also wants younger Dentist to be his successor but younger Dentist doesn't have much extra cash flow today.

SOLUTIONS

1. Restructure the retirement plan to allow for 401(k) options. Put older Dentist's spouse on the payroll. Allows older Dentist to end up with \$50,000 (instead of \$20,000) to be placed tax-wise into retirement plan. Cost for all other employees remains the same, but allows younger Dentist to voluntarily make his own 401(k) contributions if he wishes.
2. Enter "buy-sell" agreement with younger Dentist with three parts:
 - Part 1. Immediate sale of 30% of the practice to the younger Dentist for a sales price reflecting a minority discount and lack of marketability discount. Roughly 40% discount on \$120,000 portion of practice or a selling price of \$72,000. Sale financed by bank loan as older Dentist can sign the note to guarantee, as he has collateral of getting his 30% back if younger Dentist defaults. Repay the bank loan within 10 years.
 - Part 2. Deferred sale of remaining 70% at age 65 (ten years) based on agreed upon formula. In many cases the 70% becomes worth more than the original 100% as younger Dentist has incentive to grow the business as he now owns part of it. Bank will likely finance 100% of the remainder as younger Dentist already has "skin in the game" and has proven he can pay his debt under Part #1.
 - Part 3. What if the older Dentist should die before being paid? Require younger Dentist own life insurance of \$300,000 on the older Dentist. Where will the young guy get the premium since he is already cash short and must also pay for the 30%? Add a clause to the Retirement Plan that allows his account to buy life insurance on anyone that he possesses an insurable interest in. Thus use "tax wise" dollars to fund the life insurance.

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