

The Lifecycle of a Family Business Owner: Birth, Midlife Crisis, Death and Beyond!

**Business Planning Group
Spring Symposia
Thursday, May 6, 2010
Philadelphia, PA**

FACT PATTERN

Larry Johnson graduated from MIT in 1975 and, along with two of his college engineering fraternity brothers, Moe Jones and Curly Jackson, formed Microsystems, Inc. in 1976. Microsystems, Inc. was incorporated in Delaware, but its main headquarters is in Minnesota. Microsystems, Inc. elected to be taxed as an “S” corporation for income tax purposes. Larry, Moe and Curly are one-third (33%) equal shareholders, and each initially contributed capital of \$10,000 to Microsystems, Inc. in exchange for voting common stock. Larry is President and Chairman of the Board of Directors of Microsystems, Inc., Moe is Vice-President, Treasurer and a Board member, and Curly is Secretary and a Board member. Larry’s goal was to make Microsystems, Inc. a global manufacturer of cellular dial-up connectivity and business networking products. Microsystems, Inc. and its shareholders entered into a buy-sell agreement dated June 1, 1976, that provides that upon the death of a shareholder that the company will redeem the deceased shareholder’s stock at book value. The buy sell agreement has never been updated or amended.

Larry married Jane in 1978. Jane did not work outside the home, and Larry and Jane had three children: Robert, born June 15, 1980; Roberta, born August 20, 1982; and Rojean, born January 2, 1985.

Microsystems, Inc.’s growth has been phenomenal. Microsystems, Inc.’s revenue grew from \$2 million in 1978 to over \$700 million in 2010. Twenty (20) affiliated entities were formed over the years—some corporations, some limited partnerships (LP), and some limited liability companies (LLC), and all are controlled by Microsystems, Inc. The company and its affiliates hold over 100 patents. Some of entities hold real estate. Larry, Moe and Curly anticipate that company growth will continue at an annual rate of 15% over then next 5-7 years. Larry, Moe and Curly each make over \$1 million in executive compensation, and Microsystems, Inc. stock was recently valued at over \$100 million.

Microsystems, Inc.’s phenomenal growth came with much sacrifice by the shareholders. Larry and Jane were divorced in 2003. Larry and his “partners”, Moe and Curly, are constantly at odds about compensation, the composition and number of Board members, the operational and strategic direction of the company, whether it should align with other strategic domestic business partners, whether it should expand to China or other international locations, and whether it should remain private or “go public”.

Moe has two sons, both of whom recently graduated from college, one with a law degree, and one with a masters degree in engineering. Both of them have shown a strong interest in working at the company. Larry’s son, Robert, is a CPA and has been working at the company since 2003. Roberta and Rojean have shown no interest in working at the company. Both are married, and have children—Larry’s 4 grandchildren. Roberta’s husband works at the company and is very interested in becoming

an owner. Curly is single and a confirmed bachelor. In 2009 Larry married Judy, who was 20 years his junior and a graduate of Harvard University.

In 2010, Larry, at age 59, had a mild heart attack, but recovered quickly. With his health and his new marriage weighing on this mind, he is thinking more and more about retirement, and wants to explore his business succession and estate planning options. He is aware that in 2010 there is no federal estate tax or federal generation skipping transfer tax, but that there continues to be federal gift tax, as well as a stand alone Minnesota estate tax with a low exemption of \$1 million. He is also aware that Minnesota has no gift tax or a state only QTIP election. Finally, he has heard rumors that, because of budget shortfalls, Minnesota may soon have a gift tax. Larry has a second home in Florida and is spending more and more time there. He is aware that Florida has no income tax, estate tax, or intangible tax. Larry wants to treat his children equally.

Summary of Facts:

1. Microsystems, Inc. was formed in 1976 as a Delaware corporation with headquarters in Minnesota. It is an “S” corporation.
 2. Microsystems, Inc. has three (3) equal 33% shareholders: Larry, Moe and Curly, and all are Minnesota residents. All stock is common voting, and no stock has been gifted to family members.
 3. Microsystems, Inc. has a number of affiliated controlled LLCs, LPs and corporations, some of which hold real estate.
 4. Microsystems, Inc. and its shareholders entered into a buy sell agreement dated June 1, 1976, that requires the redemption of a deceased shareholder’s stock at book value. It has never been amended.
 5. Microsystems, Inc. sales in 2010 were \$700 million.
 6. Microsystems, Inc. stock was valued in 2010 at \$100 million.
 7. Larry is married to Judy—second marriage. He has three (3) adult children from his first marriage, one of whom is currently working in the company. Larry has 4 grandchildren. Larry’s son-in-law also works in the company and wants to become an owner.
 8. Moe is married—first marriage. He has two (2) adult children, both of whom are recent college graduates, and both have shown an interest in working in the company.
 9. Curly is single and has no children.
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