00:00:05 So you've decided to incorporate your business, woo hoo! Or to review the type of entity that you already chose, when you asked the people on the internet how you should incorporate, good on ya. It's important to get this right, and not rely on people who don't know you or your business to tell you what to do. Before we look at which type of entity is right for you,

00:00:29 let's look at who or what should own your business entity. This is a question that is often overlooked by basic business attorneys. And I want to make sure that you don't miss it just because they do. So let's see if it's relevant for you at all. When looking at your business to determine which entity is right for you, there are four key questions to ask.

00:00:52 And the starting place like Stephen Covey said, "Is to begin with the end in mind". So question one, what is the exit plan for the business? Which is a fancy way of saying, do you want to sell it, work in it until you die or something else? Question number two, who owns and manages the business? Meaning you alone, or you and partners.

00:01:17 Number three, who is liable for the debts and the liabilities of the business?Meaning who's taken on all the risk, and number four, How is the business taxed and how do you want it taxed? Now I know you'd prefer it to be not taxed at all, but it's going to be taxed some way so best if you choose. Right? So we'll get into the second,,

00:01:42 third and fourth questions when looking at which type of entity, but first we want to consider who or what should own your entity. Should you own your business in your own name, or should you own your business in some type of an asset protected vehicle? The answer to this question depends on how you plan to exit the business and what sort of risky business you may engage in personally,

00:02:09 such as the risks of dying or divorce, both of which are fairly typical occurrences. In fact, given that we know for certain 100% cannot avoid it, no matter what that you are going to die, sorry, but not sorry, because facing that actually supports you to make way better decisions during your life. We know with certainty that you should, at the very least own your business interests,

00:02:38 no matter whether they are interests of an LLC or a corporation or a partnership, all of which we'll look at in a future lesson, you should absolutely without question own your business, at the very least in a revocable living trust. A revocable living trust is simply an agreement between you as the grantor of the trust and you as the beneficiary of your trust to hold your assets like your business in such a way that upon your incapacity or death,

00:03:14 your successor trustee, the person you name, because you trust them and know they'll take care of your business for your family, your clients, and your team will step in and without any court involvement whatsoever handle your business affairs. Because the trust is revocable, which means that you can revoke it at any time, there is no separate tax ID. There

are no tax consequences.

00:03:41 There's nothing other than an agreement that gets created and is in place up until you become incapacitated, or when you die. Super easy peasy, if you're working with a lawyer to do it for you, who can ensure that you make the right decisions and get it handled. Now, the one downside of a revocable living trust is that there is no protection from creditors,

00:04:07 divorce or estate taxes. And if you are building a business that is not going to have a big future value and is really just a cash machine for you, earning you money, paying you for your services, paying your team, and isn't something you'll sell in the future for millions or billions, then owning your business through a revocable living trust is just fine.

00:04:28 But if you are building a business or a company that you will one day want to sell for millions or billions, or that will be worth millions or billions, when you die, then you really should not own that business in your own name at all. Instead, you should own that business in an irrevokable trust. What that means is that a trust is created,

00:04:52 that you cannot revoke. In fact, it's not even going to be created by you. It will be created for you. It does have a tax ID number. Technically it is a separate taxpayer, though, depending on how it's created, it may still be taxed at your tax rates and on your personal tax return. And that trust owns your business. And you may be the investment trustee of that trust,

00:05:19 which means that you make all the investment decisions, but there'll be another trustee, an independent trustee. And that trustee makes the decisions about the distributions. Now, you can fire that trustee and replace them with somebody else, so really you're still in control, but having that trustee in place creates a layer of asset protection and protection from estate taxes. That can be extremely valuable to you.

00:05:48 Here's the long and the short of it, if you are building a business that is just for you during your lifetime, you can and should own the whole business or your share of the business yourself inside of a revokable trust. But if you are building a business that you want to sell in the future for millions or billions of dollars, or that you want to leave behind with millions or billions of dollars,

00:06:13 a value, you may want to consider that you should actually not own that business at all. If you are not building a multimillion dollar or billion dollar business, then you can make a note in your journal, own my business and a revocable living trust and skip to the next lesson. But if you are building a multimillion dollar or billion dollar business, then listen up because I'm about to save your family some big time tax money and protect your assets from those who will want a piece of them as you become more well known for what you've created.

00:06:49 So why would it make sense for you not to own your business? Remember, in the last session, when I said that using a corporate entity is like having a bubble around your

business that protects your personal assets from your business. Well, what about protecting your business from your personal activities? If you own your business in your own name and you get into personal trouble of any sort,

00:07:16 your business could be taken to satisfy the judgment. For example, when I got divorced, I had to buy half of my business from my husband. That's a pretty common example. And here's a less common, though illustrative story. My friend Anthony was staying in his friend's penthouse apartment in New York City. His friend was out of town. So Anthony decided to run a bath for himself,

00:07:41 but then another friend called and invited Anthony to go out so away he went, but he forgot to turn off the bathtub. When Anthony arrived back at the apartment at 2:00 AM that morning, the doorman informed him of the bad news. His running bath had flooded the whole apartment and the one below to the tune of $400,000 of damage. While the insurance on the apartment covered the claim,

00:08:09 the insurance company then wanted Anthony to reimburse them under what's called subrogation. If Anthony had owned assets with any value, including his own business, the insurance company would have sued him and gotten a judgment for $400,000 and taken Anthony's business in satisfaction of the claim. So one reason you may not want to own your own business in your own name, if it's going to have significant value, is to protect your business from your personal activities.

00:08:42 In the module on insurance, we'll cover how to use insurance to protect your assets. But if you're building a really big business, you may want to consider not owning your assets to begin with. Another reason not to own your business in your own name is that one day when you sell your business or when you die, you may want the value of your business to be outside of your estate for estate tax purposes.

00:09:08 Now, currently the estate tax exemption amount is around 11 and a half million dollars, meaning that you can die with 11 and a half million dollars of assets and not pay any estate taxes. And the reason I say around 11 and a half million dollars is that it changes each year slightly, and it can change significantly depending on who's in office and how much the federal government needs to raise for taxes.

00:09:35 And while I am a big fan of plans to tax billionaires, generally, you're not a billionaire yet. And I believe based on the fact that you are here now, that if you do become a billionaire, you're going to be the kind that will use your money to benefit others and share the wealth, and not to hoard it all for yourself and build yourself a bunker.

00:09:55 I imagine you'll do better with it than funding the war machine. So right now, all estates over 11 and a half million dollars paying estate tax of 45% as recently as 2001, all estates over just $675,000 paid an estate tax of 55%. And depending on who is in office and

what the needs of the federal government are, that amount will fluctuate. And depending on what state you live in your state may have a much lower estate tax exemption,

00:10:31 such as Massachusetts, which taxes, estates over just $1 million. All that to say, if you set up your business in such a way that you are not the owner to begin with all of the value of your business grows outside of your state for state tax purposes and outside of your estate for creditor purposes, too. Meaning protection from divorce, lawsuits, and even a future bankruptcy,

00:10:58 if that becomes necessary. So if this is you and you're hearing this now, and you already own your business, it may not be too late to move it out of your hands and into an irrevocable trust structure, but you'll definitely want to get on the phone with a trusted lawyer who understands these structures as soon as possible and get planning. And if you have not started your business yet,

00:11:21 but you have a great deal of confidence that you are building a business that you will sell for millions or even billions of dollars in the future, or that will be worth millions or billions of dollars when you die, then call up your lawyer too, and before you incorporate your business with you as the owner, ask about having one of your parents set up an irrevocable trust for you.

00:11:44 That can start your business in a way that has you not even own it to begin with. That's the most airtight form of asset and estate tax protection that you can get through legal planning. Alright. That takes us through who should own your business, and I'll see you in our next session.