



Personal Financial Planning for Business Owners



Financial Planning for Business Owners

Personal financial planning is a critical aspect of managing your finances when you own and operate a business. It involves creating a comprehensive financial plan that takes into account your personal financial goals and the unique financial challenges and opportunities that come with being a business owner.

This overview will give you a basic understanding of how financial planning can help you, your family and your business, including:



The reasons to create a financial plan



Special considerations for business owners

Reasons to Create a Financial Plan

Financial planning creates an overview of all areas of your finances – cash flow, investments, tax planning, insurance, retirement planning, and estate planning – in the context of your business to make sure they work together to pursue your goals. Having a solid plan in place is particularly valuable to business owners for the following reasons:

Separation of finances

Many business owners mix personal and business finances. However, doing so could compromise some aspects of your finances. For example, let's say you want to add a new product to your inventory or hire an additional salesperson. What if you also want to add funds to your child's 529 college savings plan? Which takes priority?

A financial plan can help you anticipate such scenarios and establish a practical balance between pursuing your business and personal financial goals.

A financial plan helps in maintaining a clear separation of your finances, including:



Personal and business cash flow



Personal and business investment accounts



Personal debt versus any debt you take on as part of running or growing your business

With debt or other liabilities, it's especially important not to put yourself in a position where your personal assets could be exposed to creditors.

Protecting your family's goals and legacy are the most important things to keep in mind, especially if your business should fail at some point. While it's difficult to think about, it's something you have to consider.

Wealth accumulation

A well-thought-out plan can help you build personal wealth by guiding your investments, minimizing taxes, and managing debt effectively.

Guiding your investments

It's important to keep in mind that your business is one piece of your larger personal investment portfolio. Being in business represents a significant risk, even if it seems like you're currently in a safe industry or dealing well with economic challenges. On the other hand, as your business grows and expands, it could potentially become an oversized proportion of your net worth. Your financial planner can advise you on creating an appropriate risk diversification strategy that takes into account all the assets in your personal investment portfolio.

Minimizing taxes

The tax planning process can help you determine the best way to structure your business to minimize federal, state, and local (if applicable) income taxes. Sole proprietorships, partnerships, S or C Corporations, and LLCs or LLPs have different income tax requirements and tax calculations. A financial plan will also build in projected Social Security and Medicare taxes, unemployment taxes, excise taxes, sales taxes, as well as withholding or estimated quarterly tax payments you may need to make.

Managing debt effectively

This will be critical to your ability to build personal wealth. Many owners invest in their businesses using personal funds, which may be appropriate in certain situations. However, using your own capital, or personal credit cards, places you at significant personal financial risk if something happens to the business. Just as you would diversify your investment portfolio, you should also diversify your business funding options. The Small Business Administration is an excellent resource for business owners, not only for information and guidance, but also for low-interest business loans.

Risk management

Running a business involves various financial risks. A financial plan helps mitigate these risks by ensuring you have personal financial stability even if your business faces challenges. In general, it's important for every business owner to obtain and maintain various insurance coverages such as:

Liability insurance

The type of liability insurance you need depends on the industry you're in, and liability laws are constantly changing.

Property insurance

Review your coverage to make sure it reflects recent building improvements or additional property. Determine if the coverage will rebuild or repair according to current building codes, and if it will cover replacement costs at current prices, or only at a set limit or depreciated value. Also learn what kind of disasters your insurance will or won't cover. You may also want to consider whether inventory coverage is appropriate for your situation, as well as additional personal umbrella insurance coverage.

Business interruption insurance

This insurance covers lost income and overhead expenses when a business must temporarily close its doors due to a covered disaster.

Life and disability insurance

Businesses frequently provide this coverage to employees as a fringe benefit. Business owners also may need life and disability insurance for business purposes, such as collateral for a loan, to fund a business succession plan, or to mitigate the loss of a key person – including yourself.

Health insurance

Health insurance premiums have become a major expense for business owners, but there are ways to keep costs under control and still offer this important benefit to your employees (and yourself). One example: establish a less expensive, high-deductible health plan and supplement the plan with a tax-advantaged health savings account (HSA). Employees' contributions to an HSA are tax deductible, and tax-free distributions can be used to pay for current medical expenses or save for future health insurance premiums.

Other insurance needs and strategies

Depending on your needs, there are more complex insurance coverage strategies you may want to consider, including:

- **Buy-Sell Agreements:** a legally binding contract that stipulates how a partner's share of a business may be reassigned if that partner dies or otherwise leaves the business.
- **One-Way Buy-Sell Agreements:** a legally binding contract between the sole owner of a business and someone who is not currently an owner, whereby the non-owner becomes an owner upon certain events (such as death or disability of the owner).
- **Split Dollar Life Insurance:** an agreement between two or more parties to share the ownership, costs, and benefits of a permanent life insurance policy.
- **Key Person Life Insurance:** a business life insurance policy taken out by a company to help protect against financial loss if an owner, partner, top executive, or essential employee passes away.

Your financial planner can explain these strategies in more depth.



Reality check

What if you become seriously ill or pass away? Will your partners or others be able to continue managing the business effectively? Will the revenues support your family? A financial plan forces you to consider such worst-case scenarios, identify how much income is needed to support your family's financial needs in your absence, and implement strategies to provide that income.



Succession planning

Business succession planning is essential for anyone who owns a business because typically the business is the largest asset in the owner's estate. This is not just a tax issue. Without business succession planning, it's unlikely that your business will survive to the next generation or sell for its true value (assuming that succession or sale is the goal). There are a number of things to consider with succession planning. For example:

- Do you want to pass the business on to your children or other family members?
- Do you want to provide a path for partners and key employees (who might be most knowledgeable about your business) to take over?
- Or some combination of both?

A financial plan can help outline your wishes and provide sound strategies to make them a reality.

Retirement planning

Many business owners don't save for retirement because they believe they'll be able to sell their business and live off the proceeds of the sale in retirement. However, most overestimate what their business might be worth, especially when looking decades into the future. A number of unforeseen events can affect the value of your business over time, including:

- Changes in technology
- Customers leaving
- New competitors taking away market share
- Many other potential events

Recent legislation (known as the SECURE Act 2.0) increased the tax incentives for setting up a 401(k) plan. In many cases, the tax incentives may be enough to cover the traditional costs associated with starting up a plan.

A personal financial plan can help you save for retirement and work toward a secure financial future.

When it comes to establishing a company retirement plan, many business owners feel it's too expensive or complicated. However, sponsoring a quality retirement plan is an important part of being able to recruit and retain talented employees. A wide selection of plans are available, such as:

- 401(k) plans
- Profit-sharing plans
- Simplified Employee Pension Plans (SEP)
- Savings Incentive Match Plan for Employees (SIMPLE)

There are also a number of retirement saving strategies that help minimize your taxes in retirement, including:

- Diversifying your savings between traditional pre-tax contributions and after-tax (Roth) contributions
- Converting a traditional pre-tax retirement savings account to a Roth IRA

Your financial planner can educate you on the various strategies and help you determine which approaches might be appropriate for your situation.



Seven steps financial planners follow

- 1 Understand your personal circumstances
- 2 Establish goals and objectives
- 3 Gather financial data
- 4 Analyze your financial status
- 5 Develop a financial plan
- 6 Implement your financial plan
- 7 Monitor and adjust

Special Considerations for Business Owners

For business owners, there are many factors to consider and plan for. The following questions can help you organize your thoughts and prioritize your current needs in preparation for meeting with your financial planner.

Questions to consider

- Does anything in particular worry you about your finances or about the business's finances?
- Are taxes a big concern?
- Do you know how much income you will need when you exit the business in retirement or before?
- What are your biggest concerns for the business? For your family?
- What are your personal goals for yourself and your family? What are your goals for the business?
- How is your business helping you build wealth and provide for your family? Do you expect it to continue indefinitely, or do you anticipate changes?
- What challenges are impacting your business or personal goals now and potentially in the future?
- What tax planning strategies have you implemented so far to reduce your personal tax liability?
- How are you helping yourself, along with any partners or employees (if applicable), in saving for retirement?
- How have you funded the growth of your company? Do you have outstanding business-related personal loans or guarantees?
- Do you have a key-person and a key-customer contingency plan in place? What would happen with your business if something happened to you or a key member of your team, or if you lose a significant customer?
- Regarding your liability protection, what types and coverage amounts do you have in place personally and for your business?
- What strategic planning recommendations have you received regarding future ownership of your business?
- In terms of succession planning, what is your plan for your ownership interest in your business: do you plan to pass ownership to family members or partners or arrange for a sale?
- What method(s) have you used to assess the value of your business and how confident are you in the valuation?
- Is your business insurance still sufficient to ensure the business can continue to thrive after your death or disability?

See following page for important disclosures.



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Sources: Kiplinger (2): Financial Health Checklist for Small Business Owners; Financial Planning for Small Business Owners; Certified Financial Planner Board's Code of Ethics and Standards of Conduct (Section C: "Practice Standards for the Financial Planning Process"); Financial Planning Association: Financial Planning and Your Small Business; U.S. Bank: Financial Planning for Business Owners.

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