Winery and Vineyard Succession Planning

By David A. Holstein, Esq. and Erika H. Hooker, Esq.

While the vineyard is still quiet and contemplating the end of winter, now is the perfect time for New York wineries to be considering succession planning. Are there family members ready for more responsibility? Key employees you want to reward going into the next harvest season and beyond? Are you at an age where Medicaid planning is important?

Business succession planning simply means having a list of objectives for the future that are achieved through legal agreements. Below are some critical issues every winery and vineyard owner should consider when thinking about and planning for the future of the business.

Business Structure

The structure of your winery business is a key vehicle for transferring the business to the next generation of owners. What is your current business structure? This could be a limited liability company, a corporation, a partnership, a sole proprietorship, etc. Each has its own advantages and disadvantages, and none are "wrong". It is vital to take a critical look at your business and see what kind of protections, transference options, and tax implications are important to you and place your business in its most competitive position.

Starting with the simplest form, a sole proprietorship is just you. There is no separate entity, and thus, there is no liability protection. There are no filing requirements with the State, but you can choose to file a "Doing Business As" certificate in your county clerk's office if you have a different business name.

A general partnership similarly offers no liability protection; this is when two or more people engage in a business for profit. Keep in mind, you are jointly and severally liable for all debts or liabilities of the partnership. This means that regardless of each individual's responsibility for anything that goes wrong, someone could collect everything from you alone.

Limited liability companies (LLC) are separate entities formed under New York State law. They have become much more popular with agriculture businesses in recent times because they lack many of the formalities of corporations but still offer liability protection for their members.

If an LLC is owned by one person, operationally it is similar to a sole proprietorship, but it provides liability protection. The LLC is disregarded for tax purposes and all income and expense is reported on your individual tax return.

If the LLC is owned by multiple parties, the members can choose to have the LLC taxed as a partnership or as a corporation. If taxed as a partnership, the income and expenses of the business are passed through to your individual tax returns. The benefit of being considered a partnership for tax purposes is that your winery business is only taxed once, at the individual level.

Corporations are also formed under New York State law. Unlike LLCs, income of corporations is taxed at the corporate level and again at the individual level. Essentially, the same income is taxed twice. However, corporations may make an S election, in which case most of the income passes through to the shareholders and is not taxed twice. As with LLCs, corporations offer greater liability protection to the individual owners than sole proprietorships and general partnerships.

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Again, there is no one size fits all approach to choosing the right structure for your winery or vineyard. You may even choose to have multiple structures or entities; one entity might hold the operating business, and another could hold the land. This helps to separate assets and limit liability further. Thinking about your business goals and discussing the options with your team, including your attorney, accountant, insurance agent, and advisors, will help you make the right decision for you.

Business and Non-Business Heirs

Who are the current owners of the winery and how does the business structure help or hinder? If it is the senior generation, how do you plan to transfer ownership and control to the next generation? This must involve consideration of your goals for the business as well as your desire to provide for your heirs.

Many wineries find themselves in the difficult position of having business heirs and non-business heirs and more liquid assets tied up with the business than readily transferable ones. It often is impossible to be equal among business and non-business heirs, but it may still be possible to be equitable. Consider the sweat equity already built up by business heirs prior to their buying in or being gifted interests in the business. Consider utilizing life insurance, investment assets, non-business real estate, and retirement assets to create a more equitable inheritance for those heirs not involved in the winery.

Consider too your non-family partners and key employees. How will you incentivize them to stay in the business? Balancing these relationships is tricky and can be addressed through careful succession planning.

Transfers

Once you have picked the appropriate vehicle to house your winery business, the actual transfers of ownership interest must be thought out. There are gift, estate, and income tax implications for any transfer of ownership.

Currently, there is a federal gift and estate tax exemption of $11.58 million, adjusted yearly for inflation. If properly planned, a married couple can transfer twice that amount, $23.16 million, through lifetime giving or at death, before federal gift or estate tax will be due. The New York estate tax exemption is lower at $5,850,000, also adjusted yearly for inflation.

Unless extended by federal legislation, for transfers after 2025 the federal gift and estate tax exemption will drop back to the rates in effect prior to 2018, adjusted for inflation. This amount will be equivalent to the then available New York estate tax exemption and will be roughly one-half of the amount of the federal exemption that was available in 2025.

These limits are sufficiently high enough for many people not to be concerned with gift and estate taxes. However, if you do have assets greater than these exemption amounts, the temporarily high federal gift tax exemption provides an opportunity for winery owners to transfer substantial wealth to succeeding generations with no gift or estate tax impact. A gift within the exemption limits will forever eliminate federal gift and estate tax on the gifted assets. If you survive the making of the gift by 3 years, New York estate tax on such assets will be eliminated as well. However, your heirs will have a carryover basis in the assets gifted. If instead you hold the property until death, the heirs will obtain a step-up in basis in the inherited assets. The built-in gain of inherited assets will never be taxed on a subsequent sale, while the built-in gain of gifted assets will be taxed.

Use of Trusts

Transfers to individuals can be outright or in trust. Among other benefits, a trust will protect the asset from the creditors of the trust's beneficiaries, including a spouse of a beneficiary in the event of the beneficiary's divorce. In conjunction with this, you may want to maintain control of the business yet transfer some current value and future growth to the next generation. Recapitalizing the business entity to allow for a small percentage voting interest, to be retained for yourself, and a large percentage non-voting interest, to be passed on to the next generation, is one way to achieve transfer of ownership while maintaining management control.

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Transfers to a trust with the right language can also help you qualify for Medicaid if you are concerned about paying for nursing home care in the future. If you do not have long term care insurance, this kind of planning is vital to protecting your winery business interest for the next generation yet still have income to live on in retirement.

Buy-Sell Agreements

What agreements do you currently have to effectuate all these transfers? Having a buy-sell agreement in place helps put into operation the appropriate transfers of ownership you desire. These agreements should be created when structuring your winery's different entities but can also be amended at any time. Buy-sell agreements accomplish several important objectives, including providing a mechanism for orderly business succession should an owner pass away, want to retire, or become disabled. They also help to restrict outsiders or unwanted business partners from becoming owners.

The agreement must address the method you agree to use to value the business interest, and whether there is a discount to be applied to the value in all or some (e.g., voluntary withdrawal) circumstances. The agreement must also address the method of funding the purchase, including the use of life insurance for at-death purchases, disability insurance for disability purchases, institutional financing, and business-issued or remaining owner-issued promissory notes payable to the selling owner.

Although there is a lot to consider when planning for passing on the winery to the next generation of owners, now is the time to start putting these agreements in place to ensure a smooth transition. It does not all need to happen at once but starting to think about your objectives and getting input from key employees, family members, and advisors should start today. Succession planning for wineries and vineyards requires careful consideration of the special assets of the business, who the next generation owners will be, and how to ensure the business' continued success.

Bousquet Holstein's Wineries and Vineyards team offers services addressing a wide range of issues impacting our clients' businesses, including business succession planning and related business transaction matters. We would be pleased to assist you.

Bousquet Holstein PLLC: A Partner for Wineries and Vineyards

At Bousquet Holstein, we specialize in helping privately held businesses and their owners achieve their goals. With deep experience counseling family-owned companies and other privately held businesses, our lawyers can assist wineries and vineyards from start-ups to seasoned operations. We help clients plan for business opportunities (including acquisitions and joint ventures), negotiate commercial agreements, cost-effectively resolve disputes, and provide strategic and practical advice on a wide range of issues impacting our clients' business. For winery and vineyard owners, our business services are complemented by estate planning, wealth preservation, and business succession advice, giving our clients the peace of mind that what they have worked so hard to create will endure.

Our Practice Group Offers the Following Winery & Vineyard Legal Services:

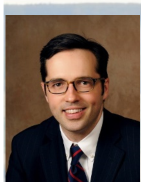
- Business formation and structuring
- Debt and equity financing
- Distribution and other commercial agreements
- Litigation and dispute resolution
- Employment, labor, and employee benefits
- Family-owned business succession planning
- ABC compliance issues
- Mergers, acquisitions, and joint ventures
- Trademark registration, protection, and licensing
- Real estate and land use
- Tax compliance and structuring
- Insurance
- Immigration, including worksite compliance

The Bousquet Holstein Wineries and Vineyards Team

Joseph J. Porcello

Ph: 315.701.6440 jporcello@bhlawpllc.com

With over a decade of experience with a top global law firm, Mr. Porcello is a versatile business lawyer who helps clients resolve commercial disputes and defend product liability lawsuits, advises clients regarding trademarks and marketing and advertising issues, assists policyholders to maximize their insurance coverage, and negotiates commercial agreements.



Gregory D. Eriksen

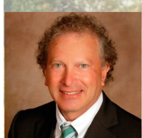
Ph: 315.701.6307 geriksen@bhlawpllc.com

Mr. Eriksen is an experienced commercial litigator with a focus on resolving the disputes of individuals and privately held businesses. His familiarity with environmental issues allows him to provide insight regarding land use and municipal interaction. As an active resident of the Finger Lakes region, Mr. Eriksen is committed to helping the area thrive.

Laurence G. Bousquet

Ph: 315.701.6383 lbousquet@bhlawpllc.com

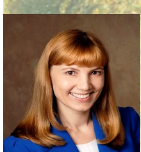
For almost 40 years, Mr. Bousquet has been a trusted adviser to family-owned companies and other privately held businesses throughout their life-cycle, working closely with clients and their other professional advisers, employees, and stakeholders to plan for business opportunities, raise capital for growth, implement acquisitions and mergers/sales, and address day-to-day operational challenges.



David A. Holstein

Ph: 315.701.6301 dholstein@bhlawpllc.com

For over 40 years, Mr. Holstein has been a sought after estate planning, tax, and business advisor to individuals seeking to preserve their wealth, pass down a family business, and maximize the value of their companies. He has counseled a wide-variety of clients who own and operate agriculture-related businesses throughout Central New York and the Finger Lakes Region.



Anna Putintseva

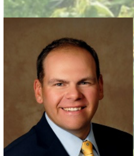
Ph: 315.701.6372 aputintseva@bhlawpllc.com

Ms. Putintseva is an experienced business lawyer who helps companies take advantage of opportunities through acquisitions, mergers, sales, and joint ventures. Her business transactions background is complemented by expertise in immigration law issues, including assisting employers and foreign nationals with preparation of employment-based petitions and worksite immigration compliance.

Jean S. Everett

Ph: 212.381.4870 jeverett@bhlawpllc.com

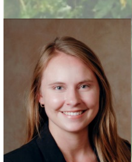
Ms. Everett works with businesses to obtain short and long-term secured and unsecured financing for their working capital, capital improvements, and refinancing needs. Jean has extensive experience with federal, state, and local financial assistance and incentives for start-up, growing, and mature businesses including tax abatement, grants, and federally-assisted loans.



Michael W. Tyszko

Ph: 315.701.6366 mtyszko@bhlawpllc.com

Michael Tyszko represents businesses and individuals in the areas of business transactions, tax planning and advocacy, economic development incentives including tax credits under New York's Brownfield Cleanup Program, and commercial litigation. His practice is centered on the core ethic of providing value to his clients by consistently being available, prepared, practical, and thorough.



Erika H. Hooker

Ph: 315.701.4425 ehooker@bhlawpllc.com

Erika is an attorney in the Trusts and Estates and Agriculture Practice Groups. A native of the Central New York region and having grown up and worked in the agriculture community, Erika has specific knowledge of succession planning for family farms. She is particularly sensitive to the complicated nature of transitioning or expanding family farms and the detail involved in such transactions. Agriculture business clients can count on Erika's unique understanding of their industry to inform her legal knowledge and assist them in coming up with the best plan possible.