The Life of an Entrepreneur

The BMO Wealth Institute provides insights and strategies around wealth planning and financial decisions to better prepare you for a confident financial future.
Entrepreneurs start with an idea; they nurture and grow that idea into a viable business. While there will be stresses and successes along the way, their business will thrive with careful planning and strategic partnerships. They will surround themselves with people who can help them grow the business and transition it to secure their future and the well-being of their family.

Back in 1984, Joe Jackson’s horn-infused, jazz-pop song1 You Can’t Get What You Want (Till You Know What You Want) was a fixture on popular radio and riding high in the Billboard charts.2 While the format and delivery of music has changed dramatically over the last 30 years,3 for entrepreneurs the message of that song is as important now as it has ever been.

An entrepreneur is much more than just a business owner. An entrepreneur is the driving force in their business; always thinking about it, innovating and making changes so that they and their business can succeed in a big way. An entrepreneur is not locked into a traditional corporate mindset where change may happen slowly and incrementally after numerous checks and balances. In contrast, the entrepreneur knows what is wanted and takes calculated risks to capture emerging opportunities as they appear in order to earn big payoffs. This entrepreneurial spirit provides the entrepreneur with the motivation, resources and financial ability to do what they want.

Interestingly, in Six Myths of Entrepreneurship,4 a lecture from the MIT Open Courseware New Enterprises course on iTunesU, entrepreneurs are defined by the qualities they do not have.

They are not:

Necessarily the highest-achieving people in their academic programs – instead they are highly passionate about things that specifically interest them and focus on those areas.

Individualists – they are actually team builders who recognize value in surrounding themselves with the right people.

Born with an innate talent for business – the skills necessary to be a very successful entrepreneur can be learned, often by trial and error.

Reckless risk takers – rather they capitalize on their in-depth knowledge, taking calculated risks in the areas where they are more knowledgeable than others and use this difference to gain competitive advantages.

Just charismatic individuals – rather, entrepreneurs have strong leadership abilities that allow them to effect necessary changes.
Undisciplined – entrepreneurs use their passion and know-how to take the limited resources they have – especially time – and use those resources effectively.

In summary, an entrepreneur must have the spirit of a pirate and the commitment of a Navy SEAL to be able to realize the success they seek.

The challenges entrepreneurs face

Entrepreneurs tend to be older and have more business experience than the average worker. According to the most recent statistics from the U.S. Small Business Administration Office of Advocacy, more than half (50.9%) of all owners of small and medium-sized enterprises are aged 50 and over and only 15.9% are under 35.

The challenge for this age 50 and over category of entrepreneurs will be to let go of the reins and transition their business to the next generation. They are likely to pass on their business to the millennials (those born between 1981 and 2000). The good news is that this most educated and least employed generation (with an unemployment rate of 15.2% compared to the national average of 6.1%) is opting for self-employment as an alternative to climbing the long and arduous corporate ladder. In the past few years, a new favorite career choice has emerged for millennials, which eclipses any other form of traditional employment – working for themselves or launching their own business. This bodes well for small and medium-sized enterprises in the U.S. and even more so for aging entrepreneurs.

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Business owners by age, 2012

Furthermore, even though most entrepreneurs are at an age when they no longer have young families, they still have considerable family responsibilities. The sometimes uneasy relationship between business considerations and the needs of the family, where both vie for the time and attention of the entrepreneur, is discussed in the October 2013 BMO Wealth Institute report The Financial Balancing Act for Business Owners.8

One of the things that help entrepreneurs to justify their deep commitment to their business is the amount of income they earn and the wealth their business allows them to accumulate. According to The Millionaire Next Door: The Surprising Secrets of America’s Wealthy, about two-thirds of all non-retired millionaires are self-employed.9 Further, according to the Corporate Executive Board Company, more than half of individuals with more than $3 million in investible assets own a business. This number jumps to 78% for individuals with at least $25 million to invest.10

But this financial success often comes at a cost. Most entrepreneurs work much longer hours than the average worker. It is reported that 63% of entrepreneurs work more than 40 hours per week, and that 10% work over 70 hours per week.11 This compares to just under 35 hours per week for the average American worker.12 Many business owners also find that running their business is stressful – they work out less, they have gained weight and are more short-tempered. But despite this level of stress, only 4% of those surveyed stated that they wanted to reduce the number of hours that they worked in their business.11

Another challenge that entrepreneurs face is establishing trust and confidence in other people’s skills, knowledge, and vision, and using these resources to help build their business. Most entrepreneurs deeply value the inputs of others in helping them make important financial and investment decisions. In fact, 62% of business owners with at least $500,000 in investible assets reported using this kind of help to make financial decisions. Only 17% reported making financial decisions with little input from financial advisors.13 Yet becoming a trusted advisor and part of the entrepreneur’s inner circle is not easy. Prerequisites for joining the inner circle are having an understanding of the entrepreneur’s business, and valuable expertise that cannot easily be obtained elsewhere.
Only the strongest and most determined survive as entrepreneurs

The odds of a new business surviving over the long run in the U.S. are relatively low. Statistics from the U.S. Small Business Administration Office of Advocacy indicate that only about half of small and medium-sized businesses survive to the five-year mark, and only one-third survive for 10 years or longer. But there is plenty of room for optimism, as some of the most famous entrepreneurs in history have had their own business missteps along the way.

Henry J. Heinz, founder of the famous ketchup empire, had an earlier bottled horseradish business fail before the H.J. Heinz Company grew to enjoy worldwide success. Colonel Harland Sanders worked in many different businesses before the creation of his KFC restaurant brand. Sir James Dyson went through over five thousand prototypes over many years before inventing the technology that made his vacuum cleaner brand famous.

Successful entrepreneurs test out new ideas, and are always trying to adapt to changes that are occurring in the world and the business environment around them.

Most entrepreneurs are geared toward making improvements in their business operations and are growing their businesses aggressively. Even with these ambitious goals and the challenges ahead of them, entrepreneurs are generally unfazed when it comes to making difficult business decisions. With all of their business experience, few feel any fear or anxiety over business decisions that they have had to make.

The need for succession planning

The survival instinct gradually becomes an addiction to continue and prosper with each year of success that the entrepreneur achieves. When asked when they might exit their business, a significant number (12%) of entrepreneurs had no plans to ever quit. As businesses survive and grow, it seems their owners tend to keep pushing out their expected exit dates. So much so that many older business owners expect to retire at a significantly later age than their employees.

This may partly be the result of a fear of the idea of retiring. The r-word is often not spoken among entrepreneurs and members of their inner circle. With so much invested in their businesses—emotionally, through their own hard

More than a half do not have a formal written succession plan.
work, and financially—many entrepreneurs envision themselves working until their last day and **dying with their boots on**, much as Errol Flynn’s character did in the similarly named 1942 movie classic. The idea of dying with their boots on is further reinforced by the fact that a majority of entrepreneurs (53%) do not have a formal written succession plan. Yet having a succession plan helps entrepreneurs feel more positive about their progress towards their business and personal objectives. Retirement is seen by many entrepreneurs as the result of running out of energy, ideas, and passion for their businesses. In contrast, many entrepreneurs who instead choose to exit their businesses early see the change as an opportunity to pursue new challenges and interests that they may not yet have had time to explore.

**The importance of the inner circle**

Entrepreneurs typically have a trusted circle of family, friends, partners, key employees, professionals and other experienced business associates from whom they seek counsel. This inner circle of confidants can be a fundamental key to the success of a business.

Entering the inner circle requires recognition of value provided and trust earned, not just once, but regularly over the long term. Loyalty is the key to joining the entrepreneur’s inner circle. Being there when needed to provide advice to the entrepreneur – and doing it well – is vital. Making it less painful and time-consuming to achieve the entrepreneur’s desired outcomes, and helping the entrepreneur get what they want goes a long way to earning trust and ultimately becoming a valued member of the inner circle.

**The balancing act of being an entrepreneur**

With all the hours that dedicated entrepreneurs invest in their businesses, the issue of work-life balance is often a potential sore spot for their families. In a recent regional survey, 75% of family business owners noted that they believe that they are able to balance the needs of the company with the needs of their family. But a significant portion of those surveyed (26%) admitted that balancing interpersonal, financial, and operational obligations can be a struggle.

There are a number of issues that keep business owners up at night. While most of their concerns often relate to

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**Most entrepreneurs make financial decisions themselves but will accept guidance from their inner circle of professionals.**
Wealth management and business banking professionals, working together with tax and legal professionals, are well-positioned to build a wealth plan that’s in line with the entrepreneur’s objectives.

A comprehensive wealth plan can help identify the business and personal needs and priorities of the entrepreneur, and address issues such as the following:

**Income options**

Being paid by salary, dividends, or a bonus has different implications for the entrepreneur and the business. Depending on federal, state and local taxes, there may be tax rate advantages in being paid a salary, but tax-deferral opportunities may be lost. Large cash payments to the entrepreneur may deplete business assets and affect lending covenants.

**Minimizing taxes**

Entrepreneurs often benefit when their personal and business tax needs are considered together. Allocating business income from an S Corporation can help to minimize taxes, especially if there are tax advantages that apply for income to be taxed personally. As the allocation of income requires that a reasonable income be paid to the entrepreneur from their

Family comes first when making future business decisions.
S Corporation, this strategy may enhance the growth of personal investment assets. But the strategy may have disadvantages for the business, including increasing the reliance on seasonal lines of credit. It is important to balance personal and business needs for the entrepreneur's greatest benefit.

**Insurance needs**
Determining appropriate methods to protect the entrepreneur, the family, and the business requires a broad knowledge of risk mitigation and of insurance-based strategies. In some circumstances it may be advantageous for insurance to be held personally rather than by the business. Alternatively, an Irrevocable Life Insurance Trust (ILIT) may be discussed with an estate attorney as part of the greater conversation around estate planning strategies.

**Minimizing risks**
Entrepreneurs by their nature try to minimize the risks that they cannot avoid. The use of ownership structures such as Limited Liability Companies (LLC) or more complex share ownership structures may limit risk and potentially help reduce future liabilities.

**Tax-advantaged savings plans**
There are a number of tax-advantaged savings options that can help the entrepreneur plan for the time when they exit their business. These options include Individual Retirement Arrangements (IRAs) and 401(k) plans. If there are concerns about higher tax rates in retirement, Roth IRAs (funded with post-tax dollars, but not taxed when making qualified distributions) may be an option for the entrepreneur.

**Investment management**
If it is appropriate to leave funds in the corporation, it may be possible to invest these amounts. Care should be taken regarding the liquidity and risk of any selected investments, especially if short- or medium-term cash needs are forecasted for the business.

**Credit management**
Being able to access credit when needed is the lifeblood of any entrepreneur’s business. Both business and personal needs must be considered when ensuring that the business maintains this ability.

**Succession planning**
This is the orderly transfer of management and ownership of a business to the next generation of managers and owners. A succession plan prepares the company’s employees, its owner, and the owner’s family for the day when the owner no longer participates in the business. There are a number of possible paths entrepreneurs, in conjunction
with legal professionals, can take when they decide to exit the business. Selling to management or a group of employees is often considered as this group will be familiar with the business and will often have interest in ownership. If an outright sale is not possible due to the financial resources of the management or employees, an Employee Stock Ownership Plan (ESOP) may allow the group to purchase the business over time and provide certain tax advantages. Another option is selling to a third party such as a business owner already in the industry. Unfortunately, the number of willing buyers is much lower than the number of businesses that are available for sale. According to research conducted on business owners that took the step of listing their businesses with a qualified business broker, only about 10% of the businesses listed were eventually sold. Given the level of financial and emotional preparedness that having a well-written succession plan brings, this is something that should be looked at closely by all entrepreneurs.

**Estate planning strategies**

Even though many entrepreneurs think that they will die with their boots on, their businesses will still pass to a successor. Planning for this eventuality means considering cash flow, liquidity, and other factors to make sure that any taxes due on the estate do not compromise the ability of the business to continue to operate.

**Taking steps to increase the value of advisor relationships**

Having a wealth plan in place helps give entrepreneurs added confidence about their progress towards their financial goals. A survey by the Deloitte Center for Financial Services found that only 52% of business owners asked had a formal written financial plan. Of these entrepreneurs, 81% were confident they would achieve their planned retirement, but this figure increased to 96% for those with a plan. Some of the positive feeling can be tied to the fact that a comprehensive financial plan includes both business and personal assets, so the entrepreneur can see their overall financial picture. Personal and business debts are also part of the picture. When a wealth management advisor and a business banking professional combine their know-how, it is possible to consider all of the entrepreneur’s assets and liabilities together to help recommend an appropriate combination of products and services to help meet the entrepreneur’s personal and business needs.

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Conclusion

There are a number of ways to help entrepreneurs achieve what they want from their businesses and from the relationships that they have built over the years. It is essential to ensure that the members of the inner circle work in harmony, always keeping the needs of the business owner in mind.

We believe that coordinated professional planning and advice go hand in hand. By working with financial professionals who understand the importance of addressing the needs of the business and the entrepreneur as a coordinated unit, the entrepreneur can receive guidance that is tailored to their individual and business needs, and that may help them achieve a financially stronger future.

Footnotes

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