

FEATURES OF FAMILY BUSINESS INHERITANCE: LEGAL RISKS AND THEIR MITIGATION

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Abstract: In the contemporary Russian economy, the issue of family business inheritance has acquired theoretical and applied significance as well, since a major part of small and medium-sized businesses (SMBs) actually function as the family enterprises, although in Russia, there is still no special unified federal law that consolidates the independent legal status of family business. In addition, this issue surely comprises three aspects of legal regulations: inheritance, family and corporate law. The lack of special legal regime for family entrepreneurship entails the application of general provisions of civil law, which do not always take into account the specific character of family ownership, personal participation in business management and the strong business dependence on the founder.

Keywords: family business, inheritance, business inheritance, succession, civil law, family law, corporate law.

Introduction: In Russia, family business inheritance does not correspond only to the deceased's property transfer to heirs, since in fact, this is an issue of transferring a bundle of assets and powers, e.g., shares in the authorized capital, shares, property rights, legal claims, managerial capabilities, business reputation, and often actual control over a business entity as well. Nevertheless, inheritance is subject to the basic principle of universal succession. According to it, the deceased's property is handed over to the heirs as a whole. Even so, unless otherwise provided by law, in the context of business, the universal legal succession often faces corporate restrictions, statutory prohibitions, the need of other participants' consent, mandatory shares, allotment marital share and the creditors' interests of the testator, etc .

The purpose of the research is to identify the legal risks of family business inheritance and suggest ways to mitigate them.

Materials and methods: To achieve this goal, the research is based on a comprehensive analysis of available sources and the application of methods of comparative legal and system analysis. The research materials included the following: current regulations of the Russian Federation in the field of family business inheritance, official explanations and government's data on the notarial settlement of succession issues in the framework of family business inheritance, a judicial practice review. Besides, the research comprised contemporary scientific works by Russian researchers on the experience of foreign countries in mitigating risks in family business inheritance.

Research results: Before considering organizational features that are related to the business transfer by inheritance, it is essential to determine the definition of a family business. Thus, in the doctrine, a business is considered a family business if three requirements are met:

- 1) ownership, i.e., the family owns a significant proportion of the company's shares or capital, allowing it to control key strategic decisions;
- 2) management, in which one or more family members are directly involved in the business management;
- 3) intention of succession, which assumes that the family intends to hand over the business to the next generations, i.e., perceives the company as a long-term, intergenerational asset, but not a temporary source of income.

Thus, the model assumes that a business is considered a family business if the family controls the property, participates in the management and intends to hand over the company to the next generations.

In Russia, the regulatory framework for family business inheritance is formed primarily by Part 3 of the Civil Code of the Russian Federation [2], which regulates inheritance issues, and Part 1 of the Civil Code of the Russian Federation [1], which contains regulations on legal entities, corporate rights, joint ownership of spouses and personal funds. The following federal laws are also of great significance: Federal Law No. 14-FZ dated 08 February 1998 "On Limited Liability Companies" (LLC) [5], Federal Law No. 208-FZ dated 26 December 1995 "On Joint-Stock Companies" (JSC) [4], "Fundamentals of Legislation of the Russian Federation on Notariate" [3]. Concerning the state registration of the corporate rights transfer, Federal Law No. 129-FZ dated 08 August 2001 "On State Registration of Legal Entities and Individual Entrepreneurs" also plays a pivotal role [6]. The contemporary model of inheritance planning is no longer limited to a traditional will, since the current law allows for a spouses' joint will, an inheritance agreement, the formation of an inheritance fund, as well as the trust management of inherited property. In Russia, the lack of a special law on family business determines the issue, in which family business is inherited not as a special object of law, but as a combination of individual rights, duties and property complexes. In other words, the law does not protect a "family business" as an independent institution, but a share in an organization, shares, an enterprise as a property complex, the legal claims to the spouses' property and the heirs' rights. On the one hand, this approach ensures the formal consistency of regulation, but, on the other hand, it forms fragmentation, since a vital single asset, i.e. a functioning family business, is legally structured into several different types of objects.

It results in the first and probably the main legal risk, i.e. the risk of corporate control loss against the family's will. If the business founder did not leave a considered hereditary and corporate framework, e.g., after his death it may turn out that the heirs are formally called upon to inherit, but do not acquire the status of LLC participants due to statutory restrictions. In turn, the Plenum of the Supreme Court of the Russian Federation clarified that in order to issue a certificate of inheritance rights, which includes a share in the authorized capital, the consent of the company's participants is not required. Nevertheless, the certificate itself serves only as a basis for subsequent resolution of the issue of the heir's participation in the company or compensation the actual value of the share. This position is crucial, since the notarization of inheritance and corporate management admission are different stages and different legal regimes [7]. The next risk is the share dilution and managerial decision when inheriting by several heirs, e.g., after the death of the owner, a share in an LLC or shares may hand over to several heirs into common shared ownership. It is evident that it does not formally violate the law, but practically leads to control fragmentation, decision-making complication and the appearance of family conflicts. Thus, for an enterprise as a property complex, the legislator intentionally provided for the heir-entrepreneur's preferential right to receive it. The division of the enterprise ruins it as a functioning business, but with respect to shares in an LLC, this issue is solved mainly proactively, i.e., through a will, inheritance agreement, statutory mechanisms and subsequent agreements of the heirs. An equally important risk is the right to a mandatory share in the inheritance, which can disrupt the pre-established business succession model. According to it, even if the owner bequeathed the business to an appointed heir, the rights of the "mandatory" heirs are preserved. The spouses' joint will and the inheritance agreement, in turn, are directly valid only insofar as they do not contradict the rules on the mandatory share and the prohibition of inheritance by unsuitable heirs. It proves that any strategy, which is related to the family business transfer to one successor, must initially take into account the range of people who can potentially claim a mandatory share, otherwise, after the death of the testator, the pre-established model will be legally adjusted.

Thus, among the primary risks of family business inheritance it is necessary to single out the corporate control loss after the death of the owner, the fragmentation of shares and managerial decision among several heirs, as well as the destabilizing effect of the mandatory share on a pre-established succession model.

Conclusions and prospects for further research: Due to the exceptionality of the legal regime of a family business, the issue of family business inheritance seems to be considered during the lifetime of the owner as a corporate security component. Formally, in

contemporary Russian legal system, there is no such general presumption, however, its introduction seems justified both from the point of view of the private family interest and from the point of view of the public interest in preserving employment, the tax base and the management succession. This idea is also supported by the contemporary doctrine. In accordance with it, current Russian researchers highlight the incompleteness of the family business institutionalization, the need for special inheritance planning mechanisms, and the special significance of maintaining a functioning enterprise as a socially and economically important asset [8].

Regarding the specific measures for reducing the loss risk of corporate control in an LLC, it is most rational to “synchronize” three documents: the charter, the inheritance document and the family and property agreement. Firstly, the charter should decide in advance whether the share can be transferred to the heirs tacitly or only with the participants’ consent. It is necessary to take into account that this issue is not to be resolved tacitly, since after the death of the owner this question causes some disputes between the hereditary title and the actual management.

Secondly, in a will or inheritance agreement, it is advisable to mention directly one business successor. As for other heirs, it is sensible provide them for property compensation at the expense of other assets. From a legal point of view, this can also be formalized either by a will or inheritance agreement. A will comprises distribution of various assets, whereas an inheritance agreement includes points about reciprocal property concessions as well as the obligations of the parties after the opening of the inheritance. It is reasonable that the formation of an inheritance fund is especially promising for large and dynastic business families, since it allows to organize a stable business management model after the death of the owner through notarized agreement’s terms.

Nevertheless, sometimes the inheritance fund easily resolves issues related not only to splitting shares between several heirs, but also the issue of allocating a mandatory share in the inheritance, since the law directly links the status of a mandatory heir with his rights as a beneficiary of the fund.

Thirdly, in case of a marriage, a prenuptial agreement or an agreement on the division of property is required to determine in advance which part of the corporate asset is matrimonial and which is included in the inheritance. Otherwise, a dispute about the marital share rises first, and only then the inheritance issue appears and it inevitably weakens management. This issue is considered in the legislative basis for in the Civil Code of the Russian Federation and the Family Code of the Russian Federation. The judicial practice of 2024-2025 proves that disputes over marital and hereditary components of corporate assets are practically significant [11].

However, the mandatory share is a main constraint on the inheritance planning freedom, since under current legislation, disabled or underage necessary heirs retain the right to at least half of the share that would be due to them if inherited by law. This rule restricts both the ordinary will and the spouses’ joint will and the inheritance agreement.

Apparently, in Russia, two legitimate ways for mitigating the risk are the most relevant: firstly, for the mandatory heirs to form a separate property framework outside the key business asset. Secondly, if there are grounds to raise the issue of applying paragraph 4 of Art. 1149 of the Civil Code of the Russian Federation, allowing for a mandatory share reduction or a refusal to assign it taking into account the property status of the parties and the purpose of the disputed property

It should be noted that this practice is implemented in foreign legislation, e.g., in Italy there is a “patto di famiglia”. It is a special “family pact” regulated by articles of the Civil Code, which allows an entrepreneur to transfer an enterprise or a controlling stake to one or more descendants during his lifetime as part of a notarized agreement specifically aimed at preventing future disputes between the heirs. In particular, the Italian Ministry of Justice states that this mechanism is developed to prepare for succession and protect businesses from subsequent conflicts [9].

The Japanese experience in resolving family business transfer issues, in turn, is specific on the other hand: government policy in the field of “business succession” has long assumed that business succession is required to be planned in advance. The official materials of the Japanese agency for SMBs prove that the successful enterprise transfer is related to the early successor preparation and the systematic process support. Obviously, the Russian legislator cannot tacitly borrow foreign models, but he can accept their fundamental idea, according to which the issue of family business succession needs to be resolved not “post mortem”, but “inter vivos” [10].

Based on the above, it is significant to conclude that for contemporary Russia, the most advantageous approach is not the idea of forming an abstract “special regime” for family business, but to consolidate in legislation the presumption of a mandatory hereditary settlement. This hereditary issue comprises dispositive tools, e.g., a will, an inheritance agreement, a prenuptial agreement and, if necessary, an inheritance fund, consolidation the mechanism of temporary business management for the transitional hereditary period. It is assumed that this framework will enable to largely mitigate the risks, which are considered in the research.

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