CASE STUDY

Intrafamily Transitions in the Business

Overview

- **Business:** Family-owned dealer of high-margin building materials with an 80-year history. Run by an experienced owner with decades of experience leading the company. Two of four children work in the company.
- **Challenge:** Family businesses come with unique challenges — namely, children work for the business in varying capacities and equity concerns for the children not in the business. In this instance, the current owner would like to gift the business to his children while minimizing familial strain.
- **Goal:** The owner wants to pass the company to the children within the business, while not excluding his other children from future inheritance. Additionally, he is concerned about the lifetime gift exemption and wants to ensure he does not have unintended tax or legal consequences.

The Opportunity

- The owner is looking to transfer the business to his two children who work for the company. One will take over day-to-day management while the other will continue to lead a department. The owner realizes that he will need help with this transition, especially since he also has children outside the business.

The Solution

The first step is understanding the owner's short- and long-term goals for the business and his family.

1. Ownership Goals: The owner wants his son to become the majority, controlling owner of the business, while his daughter will hold a significant minority stake. He also wants to ensure his estate is fairly distributed among all of his four children.
2. Business Valuation: We conducted a comprehensive valuation with due diligence on finances, operations, and strategy. This valuation will help determine the amount of the gift, the amount of the buyout and determine the assets available for creating an equitable estate plan.
3. Tax Planning: We helped the owner understand how the value of the business fit into his current and future tax planning by showing him how to transfer and retitle assets to reduce his net worth. We also put in place a cash balance plan to allow the owner, his son, his daughter and other key employees to put away larger amounts of pre-tax money into their retirement accounts. This accelerated their retirement savings while providing a larger tax deduction for the business.
4. Estate and Business Transition: The owner plans to stay with the company for the short-term. Therefore, we designed the following strategy for estate planning:
    a. Asset flow chart with equitable distribution of the estate to all four children.
    b. Professional will and buy-sell agreement, along with life insurance policies on the three family members who work in the business.
    c. Minority interests initially gifted to both his son and daughter. Future ownership transfers will be contingent on the children's performance and will likely be purchased.
    d. Open communication to address any concerns and make the process more transparent.

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The Result

- **Ownership transfer while keeping the business in the family**: Gifts of stock and subsequent buyouts allowed the owner's daughter to become a minority owner while his son became the majority, controlling owner. The owner was able to move toward transitioning the business to his children once confident they could operate it.
- **Protect Family Net Worth:** Protect the family's financial future without causing relationship strain.
- **Smooth Transition for Employees:** The open communication helped employees feel more comfortable with intrafamily transition and the expectation for continued stability.
- **Reduced Tax Burden:** Proactive tax planning allowed us to help increase the net worth of the company's key employees while also reducing the potential tax liability of the owner's estate.

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