TRANSITION PLANNING:
Keeping Business in the Family

Should I transfer my business to my family, and if so, how? What challenges must I address?

By Mike Ferraro

In the last article, we talked about why business owners should plan for succession on their own terms, not in response to a crisis. This time, let's focus on what happens when the plan is to keep the business in the family.

It sounds simple enough. In practice, it rarely is.

Start with the most basic question:

Do your children actually want the business?

Many lumber dealers assume their kids will come back after college or a few years on their own. Sometimes that happens. Often it doesn't. Some choose different careers. Some don't want the early mornings, weekend emergencies, or the responsibility that comes with keeping yards stocked and customers happy.

There's nothing wrong with that—but it does change the plan.

If no one wants the business, forcing the issue usually creates frustration for both generations.

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If one or more children do want in, the next question becomes financial:

Can you afford to give the business away?

From a tax standpoint, gifting shares can be attractive. It can reduce your taxable estate and shift future appreciation to the next generation. But gifting only works if you don't still need the income from the business.

For many dealers, most of their net worth is tied up in the company—inventory, yard facilities, trucks, equipment, and often the real estate under the operation. If you still rely on distributions to live, a full gift probably isn't realistic.

Some owners look at alternatives such as:

- Salary continuation or deferred compensation arrangements
- Partial redemptions over time
- Or, in certain cases, selling shares to a trust in exchange for payments, while moving future growth out of the estate

Each approach comes with different income-tax and estate-tax consequences, so this is an area where good planning can make a meaningful difference.

Next comes leadership.

Who's actually going to run the company?

The oldest child isn't always the right choice. The best operator might be the youngest—or none of them.

Running a lumber business requires more than knowing products. It means managing inventory turns, credit risk, vendor relationships, pricing pressure, and seasonal cash flow swings.

Ask yourself:

- Who has earned the respect of employees, vendors, and contractors?
- Who understands the numbers, not just the yard operations?
- Who can make tough decisions when margins tighten?

"Many family businesses benefit from an outside advisory board—people who understand the industry but aren't emotionally involved."

Many family businesses benefit from an outside advisory board—people who understand the industry but aren't emotionally involved. Independent voices can help keep discussions objective when family dynamics start to creep into business decisions.

Then there's the issue no one likes to talk about:

What about the kids who don't work in the business?

Putting non-working children on the payroll is usually a mistake. It creates resentment and undermines the credibility of the working management team.

If some children work in the business and others don't, it's often better to use other assets—life insurance, investment accounts, or non-operating real estate—to balance things out.

If everyone will own shares, be clear about the difference between:

- **Pay for work,** and
- **Return on ownership**

Working children should receive fair-market compensation. Ownership returns should follow ownership percentages. Mixing the two almost always leads to conflict.

Another area that deserves attention is governance.

How will decisions get made when you're not there?

If ownership is split evenly, what happens when there's a disagreement about opening a new yard, taking on debt, or selling the real estate?

Some owners keep voting control while transferring non-voting shares. That can work for a while, but eventually control has to be handed over—and it's better to plan for that than ignore it.

Finally, a reality check.

Not every family business should stay in the family.

If there's no capable or interested successor, selling to a strategic buyer—or in some cases private equity—may be the best option for the owner, the employees, and the customers who depend on the business.

If that's even a possibility, tax planning becomes critical. How inventory is valued, whether real estate is inside or outside the company, and how the sale is structured can dramatically affect what you keep after taxes.

We'll dig into those issues in the final article, which will focus on planning for a sale to an outside buyer and how to position your business—and yourself—for the best result. LC

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