CALAMOS
WEALTH
MANAGEMENT

FAMILY MATTERS

Insights on key topics—
through a multi-generational lens.

TOPIC:

KEEPING THE FAMILY IN FAMILY BUSINESS

Family businesses can be a source of tremendous satisfaction and wealth—but also of pain and strife.

How do you plan for transferring a business to the next generation? What's equitable among children? Are you taking the steps you need to now to avoid unintended consequences for you or your heirs? This installment of Family Matters is essential reading for anyone who has built a business—and wants to ensure a smooth transition while preserving value and maintaining family harmony.

We created the *Family Matters* insight series to spark ideas and spur conversation among family members on a wide range of important financial topics. They're purposely written as a primer for more in-depth discussions with your Calamos Wealth Management advisor on how the matters presented will apply to you and your family's unique situation. We hope you find that the multi-generational lens by which topics are presented promotes pass-along readership to multiple family members. Your Calamos Wealth Management advisor is available to all members of your family to provide guidance on matters you care about most.

Surf or turf? Given the choice, all three Lacovara kids have their feet firmly planted on the ground. While Mark and Angela each spent summers unloading boats at the family business, Lacovara & Sons Seafood, both pursued business degrees and, after cutting their teeth at big real estate firms in the city, joined their mother's firm, Down East Properties, and helped her build it into a powerhouse commercial real estate brokerage spanning from Gloucester, Mass., to Portsmouth, N.H. As for their mathematician brother, Robert (aka "Bob-the-Brain"), it was no surprise to anybody he wanted nothing to do with either of the family businesses.

The demographic squeeze on family business

Nearing their mid-60s, Angelo and Jackie Lacovara face two challenges—transferring one business to two of their three kids, while liquidating the other. It's a tall order but, after sharing their story with other entrepreneurs of their generation, they realize how fortunate they are to have two children who are willing and more than able to take over the real estate firm.

The numbers are eye-opening and point to what will become a massive number of family businesses changing hands in the next two decades. Every day, some 10,000 American Baby Boomers retire and, according to U.S. Census Bureau data, Boomers own two out of every three businesses in the U.S. According to calculations from research firm IBG business, if an equal number of Boomer business owners attempt to sell their companies each upon turning 65, a staggering 210,000 businesses will be hitting the market every year until 2030[1].

Three deal "dos" & one big "don't"

After working with dozens of clients to sell their family businesses, Calamos Wealth Management's Scott Poulin has seen his share of good deals and bad deals. He offers several tips:

» **Do consider getting an expert valuation;** hiring a third-party valuation firm to conduct an analysis before embarking on a sales process will set expectations and can highlight areas of the business you might want to improve before launching the sale.

» **Do get your docs in line and online;** no matter what the industry, today's buyers—as well as the deal professionals you'll be working with—expect every important document to be available in digital format.

» **Do know your buyer types;** a "financial buyer" such as a private equity firm can usually move quickly and will often leave key employees in place, at least in the near term. However, the tradeoff is often a somewhat lower price. On the other hand, a "strategic buyer," such as a competitor or a company looking to expand its activity to your industry, might be willing to pay more. With this type of buyer, the sale may take longer.

» **Don't skimp on expertise;** most business owners have one shot at monetizing their life's work and that is not the time to go it alone. Your team should include a top-notch CPA and a strong corporate attorney who, in turn, has tax and contract lawyers at his or her side. You might also engage an investment banker to help maximize the value of your sale. "Business brokers" are another option, but we usually avoid them because they tend to deal in volume, blasting out deal sheets to hundreds or even thousands of contacts in hopes of finding a buyer. They typically charge a steep fee should they get lucky.

[1] "Where's the Business Selling "Tsunami"? Dan Roth, Managing Director, IBG Business (https://ibgbusiness.com/wheres-the-business-selling-tsunami/)

But, aren't family businesses usually passed along to the next generation? "Not as many as one might think," says Scott Poulin, Senior Wealth Advisor at Calamos Wealth Management in Coral Gables, Fla. Poulin notes that many members of the generations that succeeded the Boomers are not prepared to take the reins from their parents. "They went off to college and built careers of their own or, alternatively, they just don't have the skills or personal discipline to effectively run a business," he says. In 2016, the U.S. fertility rate fell to 1.8 births per woman versus 3.7 in 1960[2]. This supports Poulin's observation that smaller families have the odds of finding a suitable successor sitting across them at the dinner table working against them.

A tear-free liquidation

Selling the seafood business built over four generations of the Lacovara family will be tough for Angelo. But, if there is one thing he has learned from managing a warehouse and dealing with scallopers, hook-boat captains and lobstermen: In business, your emotions are more likely to get the best of you—more so than any actions from the competitor across the street.

"If you think selling a home you've lived in for 20 years is tough, try selling a business that's been in your family for 50 or more years—that is excruciatingly difficult," says Poulin. But while it's difficult, he says business owners who put off the decision—perhaps hoping that one of the kids will magically step up to the plate—are not doing anyone any favors. After all, if there is no one in the family prepared to run the business after the current owner is gone, is it reasonable to think they can do as good of a job as the current owner can of liquidating it?

Poulin recalls one client who died and left his family what they all believed was a valuable business, only to learn that it came with some huge environmental liabilities they had to sort out—or, more accurately, had to bring in a coterie of expensive lawyers and consultants to sort out. In this case, the late owner—who knew where all the chemicals were buried—would have done his family a favor by liquidating the business before he died.

There are options if an owner has no heir-apparent but isn't ready to retire and wishes to stay involved. The owner can identify a buyer or structure a sale to employees and include an earn-out provision that allows him or her to remain with the company for as long as desired.

Passing it on

Jackie Lacovara is known for her big heart and she loves all three of her children. That's why thinking about how to keep Down East Properties in the family when just two of them wish to be involved makes her head spin.

Family dynamics are usually the toughest obstacle when handing down a business to the next generation, says Terry LaBant, Director of Wealth Strategy Services at Calamos Wealth Management in Naperville, Ill. Most people have heard horror stories about families ripped apart over a relatively straightforward financial inheritance. When a successful family business in which some kids might have invested significant sweat equity (and others, not so much), is part of the estate, the conflicts can become especially bitter. LaBant recalls one situation where the division of a family business dredged up issues and resentments that had been simmering since junior high, rendering constructive dialogue almost impossible. Ultimately, a business psychologist had to be engaged to help the siblings overcome their issues and get on with the business of crafting a succession plan.

[2] Vital Statistics Rapid Release Report No. 002 June 2017 Births: Provisional Data for 2016 U.S. Department of Health and Human Services, Centers for Disease Control and Prevention National Center for Health Statistics. National Vital Statistics System – June, 2017 (https://www.cdc.gov/nchs/data/vsrr/report002.pdf)

Not all families need a therapist, but LaBant doesn't discount the challenges all family business face when it comes to succession, especially when there are multiple children who may or may not be interested in playing a role going forward "The good news," says LaBant, "is that it's still possible to create and execute a succession plan that acknowledges some kids will be treated differently, even as all of them are treated equally."

According to LaBant, one of the most effective tools for smoothing over the competing interests of siblings in a succession scenario is life insurance, oftentimes coupled with a buy/sell agreement. A large insurance policy on the owner's life, with premiums paid by the company, can serve to make a sibling who is not involved in the business whole for his or her share of the company. Insurance has other uses in succession planning, LaBant says. He points to the example of the Wrigley family in Chicago, which was forced to sell its majority ownership of the Cubs baseball team and their stadium, Wrigley Field, in order to cover the tax bill when the family patriarch died. "Some better planning and some insurance to cover the tax liability could have resulted in a different outcome," LaBant said.

There's often a role for insurance even if there are no children interested in taking over the business. LaBant notes that life insurance can be structured for the benefit of key employees to help them buy out the insured individual's family when the time comes.

Today, keeping the "family" in family businesses is becoming a bygone tradition. However, the financial value and legacy to which a successful business sale or transfer can contribute is far reaching when approached strategically and with the help of professionals.

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