

Elizabeth Mower:

Hello, this is Elizabeth Mower, President of BEI.

John Brown:

And I'm John Brown, the Founder of BEI.

Elizabeth Mower:

Each episode, we take you into the world of exit planning. Sharing the stories, struggles and opportunities of business owners and their advisors. We'll get into this episode's conversation right after this.

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Elizabeth Mower:

Welcome everybody. Thanks for being here today. I'm here with Paul Kalra. Paul, you're an advisor in California and you spend a lot of time working with business owner clients, so I'm looking forward today to hearing some stories that might help us. Thanks for being here.

Paul Kalra:

Thank you for the opportunity. Good to be here. There are some experiences I have acquired over the years, if I can share those with the people present here today, I would love to do that.

Elizabeth Mower:

Great. Paul, you and I have been talking lately about some of the client work that you've been doing. And we were having a conversation earlier about the idea that sometimes it's our clients who didn't do planning even when we wanted them to, that teach us the most about the benefits of planning or the consequences of not planning. And you shared with me a story about a client that didn't plan and what happened with them. Can you tell me about that again and tell me where do your clients come from? Then if you're struggling to get them moving or if they're resisting planning, then what kinds of consequences have you seen from that? I think that's something that we can all learn from.

Paul Kalra:

Actually, this is a client I had talked to his parents, his mother, who was the last to go, some changes that she needs to bring in terms of the succession planning. I knew she was planning to give away the business to the other four children, but only one was involved.

Elizabeth Mower:

Okay.

Paul Kalra:

And I'll tell you more about that in a moment. But here's what happened. After that experience, and by the way, she did not follow my advice, kept putting it off. She said, "Oh well, I have an attorney working on it". "Okay. But attorneys do only so much. They might have set up a contract that the business goes to all the four children. But that's not the planning that we do." And in any case, what followed afterwards, after she passed away, has actually given me more reason to be emphatic with clients, of course, in a very polite way that they have to do something not just... I just don't go there and tell them, "Let's do some planning for the succession of your business." Now I actually feel how things can go awry in their lives, the children's lives, if they don't do something. So there is some depth to my conversation with them now because I feel it, that the wreck may be waiting to happen.

Elizabeth Mower:

And it's a big wreck sometimes, right?

Paul Kalra:

Exactly. I've seen it and that actually has taught me a lot. So here's what happened. So this lady actually had a nice business. This client has a franchise for the whole county on one printing business. When they got the franchise long time ago, they were the sole company and later on they expanded and anytime somebody wanted to open a franchise, they went through them. So, big revenue coming in. And one of the sons was involved in the business. Three others who are not.

Elizabeth Mower:

Okay.

Paul Kalra:

One of them was a nurse, one was a professor and fourth I believe was an engineer.

Elizabeth Mower:

Okay.

Paul Kalra:

All four very, very bright kids. I know all four of them. And the son with whom I have been working for a long time, just like his mother, I believe they all have pretty high IQ.

Elizabeth Mower:

Okay.

Paul Kalra:

I think maybe inherited from parents. So, as time went on, mom passed away. Four children inherited the business equally. The son, in all her good wisdom, mother appointed him as the trustee of the trust that they had set up. Over time the son knew that he has to be very fair, keep all the books and everything very clean so that there is no question from brothers and sisters whether everything's being handled in a fair manner. So he actually told the county firm, "Make sure all the books are neat and

clean." And over my meetings with him, I could also sense that he was very, very honest about dealings with his brothers and sisters.

Paul Kalra:

Time goes on. He found that every time he wanted to acquire some equipment or if he gave himself some increase in salary, there would be issues and complaints from brother and sister, "Hey, why are you buying this stuff?" Or, "You're buying cars so that you don't have... You're actually buying a car with our money."

Elizabeth Mower:

So they're questioning his decisions.

Paul Kalra:

"Something should be coming to us, this stuff going into your nice car." Okay? So it became a nightmare for him. Every time having to answer. Every little thing he did for the business he had to answer to-

Elizabeth Mower:

The siblings.

Paul Kalra:

... The siblings. Turns out that slowly and slowly he felt his hands were tied about anything he wanted to do. If you were to hire more people, then too there are questions. And they also, brothers and sisters, also start to feel that he is not really being honest with all the money that's coming in. Maybe he is siphoning off money in some ways. So he told them, "Look, come on over to my office, check out the books. They're all there for you." In spite of all his conversations with brothers and sisters that, "Here everything is all open," they kept suspecting there's something not quite right. So, the fears the siblings made in their own mind, doubts they created in their own mind actually start to destroy the relationships. Okay.

Paul Kalra:

The sister actually hired an attorney to go check things out. Okay. Attorney comes and they find out everything's all open. As time goes on, now sister says, "Sell the business. We want our money out." Okay. So, the brother says, "Look, there's nobody to buy the business because well, firstly we won't get the value for the business that it's worth. At the same time, this is my livelihood."

Elizabeth Mower:

Right.

Paul Kalra:

Okay. And so he said, "I'll buy the business from you." Now turns out the brothers and sister, they are trying to over value the business. So now this client of mine, he's in a total jam. As time has gone on, I've seen the total [inaudible 00:07:56] of relationships among the four of them.

Elizabeth Mower:

Right.

Paul Kalra:

They don't talk to each other. The last time I met them, he says, "I don't think my sister is sister, she is like my enemy. If she can hurt me in some way, she will." And brothers don't talk to him either. Okay. That's what, by not having a proper succession plan, that's what happened. Their relationships got destroyed, totally destroyed. And also he feels he could have done a lot better for the business if these roadblocks were not coming.

Elizabeth Mower:

Right. And I've seen that also with clients where there are two or three or four children and only one of them is working in the business and the one who's working in the business is a tiny bit resentful because everything that they do seems to be for the benefit of these other people who aren't even there. And then the people who are not involved in the business are resentful or skeptical because they believe that somehow their right to something is being interfered with or damaged in some way by the person who is there making poor decisions, which may or may not even be true. And I've seen that many times over, and I'm really not very supportive of business owners either intentionally during their lifetime or after their death, sharing ownership among what we would call business active and non-active children.

Elizabeth Mower:

Have you ever seen that workout well? I just don't think I have a very good example of kids working in the business and other kids not, where everybody gets along perfectly and respects each other. I don't have a lot of examples of that. Do you or do you find that it pretty much always goes badly?

Paul Kalra:

You are so right. Actually, I have never seen any situation where things worked out good. And looking back, by the way, this happened about seven years ago. Mother passed away seven years ago, and over seven years their relationship has got destroyed. Business has increased, but it could increase a lot more, and this was the damage to the business because proper succession plan had not been set up before.

Elizabeth Mower:

Right.

Paul Kalra:

And actually I talked to mother, I said, "Let's sit down and discuss how you can equalize the inheritance to all the four children and yet get the business to the child who is actually involved in the business." And she somehow felt the business, which had been in the family for 50 years, she felt she wants all the children to enjoy the fruit of their business. Okay. My counseling perhaps should have been more forceful-

Elizabeth Mower:

Sure.

Paul Kalra:

... And should have actually taken more time with her to tell her what can happen if she does not really follow through with my advice of separating business from other children who are not involved. Because the son who is working, you're right, he feels the same way, "Here I am working away and just sharing profits with them. And I share profits with them and yet they complain."

Elizabeth Mower:

Right.

Paul Kalra:

Okay.

Elizabeth Mower:

Yeah. "I'm working for their benefit." It's a very difficult dynamic and I actually see both sides of it. I don't have a judgment about it. I think I see how the son who's working in the business might feel, and I also see how vulnerable the children outside of the business might feel. The family has decided through the mom that everyone is to participate. So, that is the expectation that has been created. And then for them to not be able to feel secure in that, I think is difficult for them. And so it's not really right or wrong, it's just the way it is. And we think these family relationships maybe could have been preserved.

Elizabeth Mower:

So, if tomorrow another client comes into your office and has two or three or four children, some of them are working in the business, maybe three of them work in the business and one of them doesn't, and mom or dad or both are saying, "Okay. Well, we have these other things we want to accomplish right now so we probably can't deal with the ownership of the business. I guess the kids will just have to work it out." Then I suspect this next client who comes in tomorrow and all the clients you've dealt with in the meantime, you have a totally different conversation with them now, right?

Paul Kalra:

Totally different. In fact, my goal has been actually, I've been doing it when some client of mine says, "You know, my brother, my children, they all love each other, so they'll work out fine." And I actually put them in a real life scenario to project the future. I said, "Put yourself in the same situation. Let's suppose you were one of the children and two others, your brother and sisters, they had inherited the business. Okay? And you are working away. How would you feel that you are working away to pass out the profits to the brother and sisters? Even after you give the profits to them, they still complain, and every time you want to give yourself a salary increase they don't feel right about it, they think you are taking money away, that's rightfully theirs."

Paul Kalra:

So, I don't say it all in one long breath, but I put them in short question format. Put them in a scenario, or many times I ask them, "Let's look at another family which has four children in the family and one child has run the business." Sometimes when they see from outside in and they're able to more objectively see how things might go if they inherit... If or when parents pass away and the business is given to one child and he is sharing profits with the others. So when they see it from outside, then they start to see things in a better clear light.

Elizabeth Mower:

And what kinds of things would you do? Let's say we can go back in time and we're having a conversation with the mom and she says, "You know what, Paul, you're right. I probably should do something about this." Then what do you think would have been the likely outcome, not outcome, but what do you think you would've most likely put in place for her? Was there a good alternative to this shared ownership? Not every family has something else to divide up among the four kids, but where do you think that would have gone had you been able to convince her to take some action? What do you think the plan would have looked like most likely?

Paul Kalra:

Firstly, I would've tried to educate her in the... I would've tried to take her away from equalizing the inheritance to perhaps more fair distribution of the inheritance. Somebody who has helped you build the business, the son has been with you for 20 years, he has help the business. Okay? Business perhaps would not have been where it is if he was not part of the business. So, let's be fair. So, if the business is worth say, \$10 million, then out of that you have to ascribe a certain portion of business as his anyway. That business might not have been worth 10 million if he was not part of it. So, let's say his contribution has been worth maybe 30% of the business. So that leaves about \$7 million. Okay? Now, the seven million dollars you want to distribute equally among four children. Okay? Now you could divide the business among four, the problems arise.

Paul Kalra:

Now, otherwise let's look at your other assets where we may want to take other assets which are not business assets, put more weight on those for the three children who are not involved in the business. Let's suppose those assets are still not enough to equalize the inheritance of \$7 million. Remember, three million has already been assigned as the earned equity of the first child.

Elizabeth Mower:

Right, sort of the sweat equity, right?

Paul Kalra:

So, \$7 million, if it's not enough to divide equally among the four children, then what we are going to do is perhaps buy some life insurance on mom so that there's enough money coming from life insurance to go to the three children.

Elizabeth Mower:

Right.

Paul Kalra:

So that all of them have equal distribution.

Elizabeth Mower:

So that the fourth child can maybe get the business. And I think you made a good point, which is that once you've carved out the sweat equity for the child who's working in the business, that child goes back into the bucket [inaudible 00:16:34] four children to figure out what's fair in an allocation of the \$7 million of business value or wealth of the family that remains because that child is then just part of the

children kind of inheritance pool. So this 30% of sweat equity doesn't exclude that child. And I think you're absolutely right. That's the way I would do it too, is that they don't get kicked out of all of the other family wealth. They get their part that's connected with the work that they've done and the value that they've contributed to in the business. And then they go back into the general kind of family pool for traditional planning that says, "Okay, there are four children. I as a parent would like to take care of them in a particular way, and how can I use what I have or things that I can acquire in order to accomplish my goals for all four of my kids?"

Elizabeth Mower:

So I think that's probably the way I would do it too. And I think you're right that for each of our future clients, the story of another family is a very powerful way to sort of shine a light on these issues. And it's probably true in the case of your client that those four children did get along pretty well before all of this stuff happened. You haven't said anything about this family being in complete disarray and everybody hated each other from the very beginning.

Elizabeth Mower:

These issues tend to degrade those family relationships as you explained. And so, I'm hoping that the story that you tell here today and the story, when you tell it to the rest of your clients, has an impact and causes some movement because it doesn't take that much. It's not that hard, right, to do the planning? It's not complicated. It's just necessary to make some decisions and get it done. And so, that's the part I think that maybe clients feel like there's a lot to do or it would be difficult. But the way you're explaining it, it wouldn't have been rocket science, it just would have been some pretty simple planning that could've preserved maybe some family relationships-

Paul Kalra:

That's right.

Elizabeth Mower:

... Which, is in many cases the most valuable thing that they have even beyond the business, right?

Paul Kalra:

So right. Actually I use this particular example to explain to my other clients, of course, I don't tell them what type of business it was at all, I don't want any hint of any kind. But in general terms, a client with a business, that's how I try to tell them, and that, by the way, I have had a couple of other situations which are not different, but very different from this one. So I use one or two examples to really educate my new prospects who perhaps don't want to make the move of proper succession planning now while they're alive. So I use these examples and many times actually they have finally worked. They may not make a move the first time, but I have found when spouses sitting, two, in the meeting, it actually helps a lot.

Elizabeth Mower:

So let's get everybody involved in the conversation, everybody thinking about the possible outcomes that we're looking at and then deciding to maybe just take a few basic steps to avoid maybe a big explosion.

Paul Kalra:

Right. So when I ask them, "When your children are in their fifties and sixties, do you want them to love each other or do you want them to hate each other?"

Elizabeth Mower:

Very basic question, and I bet the answer is the same pretty much every time.

Paul Kalra:

Right. I said, "By not taking the steps today, you are sowing the seeds of friction later on."

Elizabeth Mower:

Agreed.

Paul Kalra:

"Is that what you want to do?" And most times mothers don't like that.

Elizabeth Mower:

No.

Paul Kalra:

Okay? So, that's when they start to put pressure on the husband. "Hey, let's start talking to Paul about these things."

Elizabeth Mower:

Okay. Well, I appreciate you sharing that story. One of the goals of this series is to share our stories and hope that advisors and business owners and people everywhere will hear the stories and maybe view things a little bit differently. Maybe take a step forward that they otherwise wouldn't have taken and maybe improve the outcomes. When you tell this story, if one person hears it and changes an outcome in one family business because of that, well you've got five, six, seven, 10, 20 lives that are affected by that.

Paul Kalra:

So true.

Elizabeth Mower:

So, I appreciate you coming in and sharing your story so that maybe we can improve outcomes for some others. So, thank you very much.

Paul Kalra:

Thank you for the opportunity. Glad to be here.

Elizabeth Mower:

Okay.

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Elizabeth Mower:

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