



Succession planning

Protecting the continuity
and growth of your assets

A process, not an event

Maybe you created it. Built it. Or maybe your leadership is carrying on someone else's founding vision. But today you look around the business you're running and see – a future. Something that's bigger and more enduring than the span of any one person's life. Or deserves to be.

Research has shown that only 30 percent of family-owned businesses survive into the second generation, and only 12 percent survive into the third. Non-family-owned private enterprises have comparable rates of eventual decline. Clearly, solidifying your business's future takes more than the desire to do so.

Making sure your business has the future you intend takes planning. You can't treat succession as a someday event. It's a process of asking questions, setting strategy, making plans, and executing them. And there's no single formula. This process is a fluid one, and it will be a constant work in progress.

It's also surprisingly complex, for businesses of all sizes and structures. From family issues to tax planning, from business valuation to goal articulation, it takes a variety of experiences and perspectives to make succession work. For most people, that means getting help from a team that's been there before.

Succession planning applies to the full array of private businesses, from founder to family-owned to employee-owned and other private structures. Many of the concepts apply equally to different ownership structures, but the application can vary significantly. Only you know your situation and your ultimate goals, but it takes the right team to get there.

Because succession involves so many company and personal aspects, a coordinated team of advisors can make all the difference. The advice you need to select and prepare new leaders isn't the same as the counsel you get every day from your attorney or accountant. A host of specialized skills comes into play, and the right advisory team is the one that can bring them together.

Ask yourself

What is your relationship to the business? Or what will your relationship be to the business two years from now? Five? Ten? Twenty?

When you are no longer involved, what will happen to your business?

If you're going to sell, is the business ready to change hands?

What do you want to leave behind?

How can you make your vision a reality?

What will happen to the stakeholders of the business after you're gone?



What you leave behind

Making plans for business succession starts with defining where you want that process to take the company. It helps to think of succession not as a stand-alone process, but as a bridge: It connects the vision that key stakeholders have today with the long-term success your company can attain.

The impact of a business is measured in concentric circles. Some are vitally important to their owners and no one else. Some are linked to the relatives of the shareholder group or to the people who work there. Others are tied into the community around them through tradition or philanthropy.

The aims of succession planning are as varied as the people to whom a business matters. For some, the principal goal is to lock in personal wealth. Others may place a greater value on the maintenance of family control or continued employment for the employees. In all but a few cases, succession focuses on the continued health of the business itself – setting conditions that will let it grow and increase its value. A succession plan will have to account for all of these considerations, which means finding the best balance among them.

Sometimes, the people making succession plans recognize priorities outside the circle of direct stakeholders. If you want your business to remain a fixture in the community, it may be more important to keep long-time team members on board or to provide for continued operation of particular locations.

If your plan involves an eventual transfer of ownership, there's more than one way to accomplish it – and the option you choose will have a significant effect on the company's liquidity and the new owners' prospects. Certain business structures can keep you actively involved while moving ownership to successors. If your employees are taking over, an employee stock ownership plan (ESOP) may provide tax relief and preserve team spirit, but under law it must be offered equally to all eligible team members. Then there are various forms of trusts and buy-sell agreements. Which strategy is right for the legacy you plan to create?

To be meaningful and actionable, any business succession plan starts with goals that are specific, measurable, achievable, challenging, and consistent with one another. Only when these goals are defined can you begin the work of making them a reality.

Ask yourself

What is your business worth?

Do you understand the value drivers and how to measure them?

What elements of value matter most to your successors?

Is your business an asset built to provide a given rate of return, or something to be sold off for maximum profit?

Are you willing to sacrifice net value for greater long-term stability?

If a recession is on the horizon – or closer than that – are you prepared to safeguard the value you've built up?



Driving and passing on business value

Know what you've got – and how to pass it on

Preparing for the future of your business can't just be about maintaining the status quo. Most enterprises aim to grow, and succession planning should be a part of strategic planning – not a replacement for it.

In any circumstance, driving value starts with knowing value. In succession planning, it's an important precursor to calculating the values involved in an ESOP, gift of ownership, or sale.

So start by knowing the different standards by which value can be measured. Fair market value might be the simplest yardstick, but it's often more theoretical than practical. The investment value of a business may come closer to a real-world figure, but it's influenced by hard-to-specify variables like goodwill and potential M&A synergies.

Different kinds of sales have specific effects on the value you realize from a business. For example, private equity buyers are showing increased interest in mid-market businesses, but a private

equity deal might require you and your successors to commit to a certain management structure. A management buyout, on the other hand, keeps these decisions within the current team. Strategies for driving the value of a business higher are not specific to the practice of succession planning. Innovation, increased efficiency, expansion into new markets and areas of operation, strategic partnership, and M&A decisions – they're all important on their own merits. Conversely, however, you can't plan succession without taking the growth of value into account.

Sometimes there are tradeoffs to be made: One business owner might value the continued health of the company (and the future happiness of the workforce) so much that he or she is willing to take less money out upon retirement. Another owner might place such a premium on keeping the management of the company within the family that he or she passes over more qualified successors.

When you know what your business is really worth, how to drive its worth higher, and what you intend to do with it later on, you can begin to build a strategy for business value.

Ask yourself

Do you want your business to remain in the family?
Do they?

Will family members other than you depend upon the business to fund their lifestyles? If you sell, how will it affect them?

What is your plan for dividing the business income among family members who are active in the business and those on the sidelines?

Will funding your own retirement needs dilute the business's future earnings for other stakeholders?



Family ownership and financial independence

All in the family

Whether it's five years away or 50, a transition in the leadership of your family business is inevitable. Yet a majority of family business owners who plan to retire in the next five years have not identified a successor.

It's important not only to make a plan, but to discuss it with family and other stakeholders to make sure it's one everyone is comfortable with. Or at least prepared for.

Your business is many things to many people. For a successor, it may be a career path. For an inactive family member, a source of financial independence. One decision you need to make is where your business lies on a continuum of priorities: On one end is a pure family system fueled by blood ties, emotion, and nurturing. On the other is a pure business system built on profit, wealth-building, and management by whoever is best qualified. Most businesses fall somewhere in between these extremes, and managing expectations is a balancing act. One

way to achieve this balance is to create governing structures – such as an outside board of advisors, or a formally constituted family council – that separate the “family business” from the “business business.”

And don't forget your own needs. Most business owners say they have the majority of their personal wealth tied up in the businesses they run. When the time comes, it may be difficult to strike a balance between taking wealth out and leaving a healthy operation behind. Different methods for transferring equity – such as sales, gifting, and the establishment of trusts – each have different implications for the retirement income they provide, the burdens the new owners assume, and the future success of the business.

Asking the right questions now may help save money, help drive value, and help make the business stronger. It should also encourage harmony when you decide it's time to leave.

Ask yourself

Is your succession plan based on a static assumption of certain circumstances, or is it flexible?

What happens if a death or other unforeseen event triggers a succession earlier than you've planned?

Have you gone through the terms of your buy-sell agreement? When is the last time it was refreshed?



Contingency planning

The best-laid plans

If you've got a succession plan in place, you're ahead of most other business owners. But does your plan assume that everything will happen the way you expect and when you expect – and nothing else?

The unexpected can arrive in many forms. You may have asked yourself, "What if I die?" But have you asked what happens if you lose your top lieutenant or silent partner? Or if a number of your key managers all choose to leave the company? The market could take a left turn and leave your products or service lines obsolete, as some manufacturers of technology equipment can attest. Your line of credit could evaporate. Nothing is too outlandish to happen.

One important tool in contingency planning is the buy-sell agreement. Instead of waiting until a crisis to determine how equity in the business will change hands, these binding agreements specify what will happen if certain conditions arise. The death of the owner is commonly a basis for such agreements, but other

situations can trigger them as well, such as long-term disability of the owner or other key stakeholders. Having a buy-sell covenant in place can avoid disagreement and disruption, and it pre-establishes a market for an asset whose value might be hard to assess in the middle of a crisis. One thing to consider is whether the surviving stakeholders will have enough cash to execute a buy-sell agreement at the moment it comes into play. Many companies use life insurance – payable to the buyers – to address this concern in advance.

To protect your business, your succession plan also needs to anticipate the way unforeseen circumstances might affect not only leadership, but things like tax liability and institutional knowledge. If an owner makes elaborate plans for the transfer of ownership – but doesn't leave behind a leadership cadre who knows what levers to pull – the succession will ultimately fail.

Ask yourself

Do you have a successor in place not only for yourself, but for other key leadership positions?

Do those future leaders know what's in store for them? Are they ready?

Is succession limited to members of your family? Do they need any qualification besides blood ties?

Is the rest of your organization prepared to accept the new leadership you've put in line behind you?



Leadership succession

In the wings

Sometimes it's as simple as adding “& Associates” to the sign over the door. But not often.

Choosing the people who will lead your business into the future involves a number of choices. And the top spot isn't the only one that has to be filled – second-tier leadership positions are just as important in maintaining continuity.

Before they can step in, your successors need to be three things: identified, in place, and ready. It's rare to find a company that doesn't have a gap in at least one area. The question is how to close them. That puts a premium not only on planning ahead, but also on recruiting, retention, and training.

Finding the right successor begins with defining the future leadership and management needs of your business, as well as the timeframe you should set to effectively make those transitions. Then, define what skills and knowledge the new leadership will need to work effectively toward those goals. Only with that knowledge can you begin to select and prepare individuals for their future responsibilities.

For example, a senior member of your leadership team may be an obvious candidate to succeed you. But that doesn't mean that person won't need specialized training and preparation to make the jump to the top spot. Or perhaps you've spotted someone who seems to have the innate ability to take over, but who isn't as senior or experienced as you'd prefer. How will you move that person toward the level of competence it will take to one day replace you? The future of your business deserves an approach to these decisions that draws on the best minds at your disposal.



Ask yourself

Who are the stakeholders in your business now and in the future?

Whose cooperation must you secure for succession to work the way you intend?

Are you ready to do enough letting go so that other players feel invested in the process?



Harmony/balancing the roles of different players

All of the people all of the time

Every business owner knows it's necessary to balance different interests while doing business. But in passing the business onto new leadership, maintaining harmony among disparate stakeholders is critical. It's a time when no one takes continuity for granted.

Who are the people who depend upon your business, have expectations of it, or have the right to make demands of it? They may not have veto power over your plan for succession, but they can stand in the way of your company's continued success. If you take the time to hear them out now, you and the leaders who come after you will be more likely to get their buy-in when it counts.

If you leave your leadership role and your family learns that you've handed the business over to a highly qualified employee who has the "wrong" last name, will they make trouble? On the other hand, if you pass control to a blood relative who isn't ready on the merits, will key managers or employees follow him or her the way they followed you? You can't make everyone happy, but by opening a dialogue now, you can prevent your decisions from becoming surprises. And you can take the steps needed to address competing demands.

Every participant in a succession will feel the pull of emotion. You have to face the fact that your control isn't absolute and won't last forever. Potential successors, and those whom you may pass over, will have to reconcile their dreams to your decisions. A good plan will keep emotion from overcoming practical considerations.

Ask yourself

How many ways are there to pass on leadership of a company? Which one is right for you?

How do your business profile, the market, and other factors limit and define those options?

Do you keep the business in the family? Sell, privately or publicly? Let the employees buy you out?

When is the right time to put your succession plan into action?

When you're gone, are you truly gone? Or do you retain a role?



Exit strategy

Moving on with maximum value

Exit strategy? You mean taking your coat, packing up the plants, and leaving, right? In fact, there's more than one way to change your role, and the course you choose can make a big difference in how the business moves forward.

You can pass the business on within the family. Or sell it to a private equity buyer – an option that's more flexible and workable today than in the past. Have you considered a merger or acquisition as a way to write your company's next chapter? If you sell the business, will it be to the management? Through a public stock offering? Or to an ESOP?

Relinquishing ownership and control doesn't have to mean that you disappear from the scene completely. You may remain an informal, advisory presence to the people who succeed you. Or you may adopt a formal role – as a board member, special projects manager, or even paid consultant.

Each option carries pros and cons, and the nature and situation of your business should help determine which is the best fit for you. As with any other aspect of succession planning, answering this question begins with knowing the long-term trajectory you want the business to be on.



The cost of inaction

Succession planning failure	Potential impact on business
Poor estate planning	Higher tax payments, which can limit business growth opportunities
Insufficient ownership structure	Failure to develop appropriate leadership and potential tax and expense inefficiencies
Lack of understanding of true business value	Business unable to attract buyer or investors, or undervalued
Lack of contingency planning	Forced sale or succession on terms not of your choosing
Successors not identified, in place, or prepared	New leadership not ready to take responsibility
Stakeholders not consulted and brought into the plan	Employees, family members, or other stakeholders won't accept new leadership
Legacy not articulated and mapped out	Legacy not achieved or reputation damaged
Planning for everyone else – but not yourself	Personal retirement not adequately funded
Failure to adequately plan for distributions from the company (dividends, salary, etc.)	Shareholder discontent or family disharmony challenges – expectations not met
Too little attention too late	Succession goals not achieved



The time is now

Planning for the next generation in your company's leadership is critical and complex. Any business should benefit from a forward-thinking, thoughtful process that takes into account the many things that go into succession planning – and the many things different people want out of it.

What's important is not to wait. Succession lies in the future, but succession planning is a present-day necessity. Every day that passes may reduce the number of options you'll have, and even small steps should help keep those options open.

Maybe you've built your business from the ground up. Maybe you've been a good steward of something passed on to you. Maybe your success has been based on balancing and serving the demands of private investors. Even if you intend to be the last link in the chain, there's a right and a wrong way to sell or liquidate the company. It all starts with a plan, and planning starts today.



Your next steps

Set succession planning goals that are specific, measurable, achievable, challenging, and consistent with one another – and that allow you to achieve the long-term vision you have for your company.

Consider the value of your business. What decisions might foster the kind of long-term growth and ultimate exit plan you envision?

Sit down with key stakeholders to set future leadership plans that align with their skills and interests – and your goals for the company.

Select the advisory team you trust to help you navigate succession planning and its implications for your business, family, and key managers.

Be flexible. Your plans may need to change as circumstances change. Revisit them often.

We can help

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