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MoneyTalk

Business Succession Planning

Part 1: The last test for successful entrepreneurs

A special breed of individual become business owners. They have a good idea and are smart enough and strong enough and dedicated enough to turn it into a successful business. Ironically, sometimes these same characteristics prevent business owners from passing the final test of entrepreneurship: Succession Planning.

Up to eighty percent of businesses are family owned. This represents a huge part of an economy and a staggering number of jobs. Unfortunately, around 70% of those businesses have no written plan for ownership and management succession in case anything happened to the owner or CEO.

Only one in three family-owned businesses survives the first generation of ownership. These businesses which would otherwise continue often collapse due to a simple failure to plan.

What happens when a business owner fails to plan for succession? Often, the business and business owner die on the same day and the family is hit with a series of problems at once. On top of the emotional distress caused by losing a loved one, the family has lost its main source of financial support. Further, the family must pay estate taxes which can take as much as 20% of the estate of the deceased.

This often means that the family must turn hard assets into cash. Selling cars and houses is usually not the preferred first step, but they are much easier to sell than a business. Moreover, they are likely to retain their value better than the business.

The day after a business owner dies; the car he drove and the house he lived in are still worth about as much as they were the day before. However, if he did not plan for ownership and management succession, the value of the business can drop rapidly. When an owner is disabled or dies without preparing successor management, the business is in trouble.

In the end, the business is in a crisis because everyone is struggling to do the jobs the CEO used to do. The family is in a crisis because they need cash to pay taxes on an estate that may have most of its value tied up in the business. Too often, the outcome is the liquidation of the business at fire sale prices. An otherwise strong business is lost, employees are out of work and the family does not get the full value of the owner's business.

More taxes, fewer choices and less control

Even when succession planning is eventually done, the results are not ideal because the business owner started too late. I recently met with a man who owned a stable business with around 50 employees.

He was 76 and was failing in his health. He wanted to get top dollar for his business, to insure that his second wife was taken care of for life, and to guarantee that the remaining estate would be passed on to his children from his first marriage.

Unfortunately, his choices were limited. Had he started planning five or ten years earlier, he would have had many more choices. He could have designed a plan to cash him out, take care of his wife and pass on the full value of his business to his children.

Had this man done nothing, or not survived his recent hospital stay, the business would have been shifted into the estate of his second wife. Further, his second wife would have gained control over all of his assets and could have left his daughters out of her will completely.

The longer this man or any other business owner waits to plan for succession, the fewer options they will have. Further, the amount paid to the government in taxes will increase and it is more likely that the plan will not meet his goals. Finally, and perhaps most important, control of the process will shift from the business owner to the government and lawyers.

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The final test of greatness

Planning for succession is the final test of a great entrepreneur. Generally, the successful businessman has proven himself in creating a strong business. The last test is whether he can manage and control a transition from his ownership and leadership to someone else's.

It is a delicate and sometimes difficult process. It is planning and controlling a process which, in the end, means giving up control. Doing it well can often take years.

The result, however, is worth the effort; it means stability for the family and secures the business for the future. In the end, this is often the greatest connection to immortality any of us may have: taking care of our family and a business that lives on for years after we are gone.

Three key components to successful planning

The technical components of succession planning vary greatly from business to business. But there are some common personal components which appear in nearly every successful transition.

Open, honest communication is crucial. Succession planning requires integrating the needs and expectations of the business owner, his family, the business, key management and other owners if there are any. *(Frequently, these groups overlap.)* Managers may be part owners and family members may be employees and owners. These interlocking relationships must be carefully managed throughout the planning and transition process.

The best way to keep the relationships focused on the goal of maintaining a successful business is breaking down the barriers to communication. When important participants are left out of the process, they find it difficult to support the outcome - even if it is a good one.

A second important component to successful planning is a careful, intentional process. If everyone understands the process of which they are a part and their role in it, they will feel comfortable and can focus on keeping the business successful. When participants don't know what is happening or where the business is going, they become emotionally distracted and preoccupied worrying about how they will fare in the end.

The third component of succession planning done right is objective opinions. These can come from outside advisors hired to assist in the process, or a truly objective advisory board or board of directors. The important thing here is that the business owner obtains valuable objective opinions about how well he is managing the process, how well prepared successor management is to take over the top job and, perhaps most important, competent legal advice about what technical alternatives are available to him.

A hero's farewell

If these three components of succession planning, ***communication***, an ***intentional process*** and ***outside advice***, are managed and maintained, the result can be the crowning achievement of a successful career. When a business owner has lots of technical alternatives and can take the time to prepare the business and family for what will happen, the result is a hero's farewell. This means an enjoyable retirement and a lifetime of accomplishments to look back on.

What to do now?

1. Begin your succession planning by getting a private notebook and record in it your personal "mission statement" and a mission statement for the business. What motivated you to become a business owner? What is the most important principle underlying the way the business works? These principles will guide your future decisions and help you to explain them to others clearly.

2. Go to the library and read available resources. Take notes on the important ideas that stand out in your mind. This will help insure the process works for you and that you are comfortable in selecting an option that fits your needs.

This article is extracted from the World Wide Web at: http://dept.kent.edu/oeoc/spp/articles/lasttest.htm, and adapted for the SA environment.

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