Protecting your legacy:

Why early transition planning matters

For entrepreneurs who love running their businesses and intend to do so for a long time, succession planning can feel like a distant or irrelevant concern. However, every business owner will eventually decide that it's time to make their exit—and it's never too early to consider the optimal way to do so.

Generally, business owners face four choices:

- Sell the business to a known third party like a minority partner or an employee.
- Sell the business to an unknown third party.
- Transfer or sell the business to a family member.
- Wind down and close the business without transferring or selling it.

Regardless of the decision, having a thoughtful plan in place can help protect the value of the business, ensure business continuity and help carry on the owner's original vision.

Important questions for business owners

Business owners have nurtured their companies for years, and most entrepreneurs are looking to ensure not only that their business will continue to be successful financially, but also that the legacy that they have created lives on through the business's mission and core values.

To address these dual goals when considering a future exit strategy, owners should reflect on these five factors:

Timing. When is the right time to sell? When is the right time to start informing stakeholders that you are looking to transition the business?

Family involvement. Which family members, if any, want to be involved in the future of the business? How can the business owner involve them in ways that are perceived as fair and responsible by other family members?

Effects on customers. How will the departure of the business owner affect the company's largest or most loyal customers? How can the business owner best prepare those customers for the transition? Is there a risk that they will leave due to losing the relationship with the business owner, and if so, what steps can the owner take to prevent this from happening?

Effects on employees. How will employees react to a change in leadership? What can business owners do to ensure that the best employees stay with the organization and help the new leader succeed?

Ongoing involvement with the business. Does the owner want to separate completely from the business and its new owner, do they hope to maintain some sort of ongoing relationship?

Creating a succession and transition plan

Working through the above questions is a first step toward drafting a comprehensive succession and transition plan for business continuity. In doing so, it may help to consult with professional experts—including tax, legal, and financial advisors—to develop a succession and transition plan that addresses each of these categories advantageously for the owner's unique situation.

Before starting, it's important to note that creating a succession plan isn't a one-time event; it's an ongoing process. Ideally, business owners will start thinking about their exit strategy early and then revise as necessary if their plans or circumstances change.

Additionally, remember that a succession plan is different and distinct from a retirement plan. A retirement plan should focus on how the business owner will stay afloat after leaving the company; a succession plan should focus on how the company will stay afloat. Some business owners mistakenly conflate the two, which can lead to inadequate planning. Focusing specifically on a plan for the leadership transition and its impacts can help ensure business continuity and minimize disruptions.

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Potential topics to address in a succession plan include:

- A mission statement.
- A vision for the business and the family.
- An executive summary of the company.
- Revenue projections for the next five to ten years.
- Information about the specific plan/method to transfer ownership, including a timeframe and a list of all parties involved at each step.

Preparing for new ownership

If the plan is to sell the business to a third party, starting succession planning early offers a chance to take a hard look at the company's shortcomings and how to fix them, potentially increasing the overall value of the business to make it even more profitable and attractive to buyers.

Preparing early can also allow adequate time to find or develop a new leader that shares your vision for the company and its stakeholders.

Planning for worst-case scenarios

Planning should anticipate difficult scenarios, such as economic downturns or declining business performance. Should business owners find themselves transitioning during a difficult economic period, for example, private buyers may not be as plentiful. Or perhaps a business owner may want to sell the business to a family member who doesn't have the capital to pay its book value.

Planning for worst-case scenarios helps ensure that business owners are equipped with strategies and solutions to meet potential challenges, rather than making rushed decisions in the moment.

Business valuation

Valuing the business isn't always as straightforward as owners might think, since a company's fair market value may differ significantly from owners' personal estimates. Often, when businesses hire a professional business valuator, the numbers come in lower than the owner estimated (since no CEO can imagine someone not wanting to pay top dollar for their business!). On the other hand, the company may turn out to be worth far more than the owner assumed. Either way, professional valuation is important in order to offer realistic insights for planning purposes.

Private businesses can be valued by a number of methods:

Income approach. Applying an appropriate multiple to the value of future cash flows or income

Market approach. Based on the prices obtained from the sales of similar companies

Asset-based approach. The value of assets in the business, minus any liabilities

Planning ahead is a sign of strength

A succession and transition plan is not designed to remove owners prematurely. It's there to help ensure a successful transition, someday.

Owners who believe they have decades until retirement might view early succession planning as unnecessary, but a transition plan is all about being prepared for anything, including unforeseen circumstances. Owners could, for instance, someday have health issues that force them to start thinking about stepping down earlier than planned.

Ultimately, a successful plan will ensure business continuity in the owner's absence—so planning for an ending often means that the company won't end, and the owners' legacy will live on. In other words, succession and transition plans aren't really about endings, but new beginnings.

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