Family business succession planning

10 tips for success

All family-owned enterprises reach a point that requires tough decisions about charting a path for the company's future: Who is next in line to take over? What qualifications do they need to succeed? Is legal and financial documentation sufficient in order to enable a smooth transition? Will there be hurt feelings along the way?

Succession planning is a dynamic process that addresses these questions about ownership and management transitions. Whether you plan to pass your business to a family member, employee, or outside buyer, succession planning requires thoughtful analysis, careful strategic planning, and the ability to manage family dynamics.

You can streamline the transition process by evaluating all succession alternatives early on. Understanding these alternatives and their financial implications can help guide your decision-making. This analysis can be complex, taking into account factors such as the current ownership structure, compensation practices, business expenses, valuations, tax considerations, corporate documents, and existing trust and estate plans.

No matter the path you choose, here are 10 recommendations that can help you develop a successful transition strategy.

1. Start succession planning early.

It's time to start succession planning long before you plan to retire or sell your business. This will give you and your family time to carefully consider your alternatives and lay the groundwork for a smooth transition.

Complex family businesses will likely want to begin their planning discussions several years before a change in ownership or management in order to have enough time to involve all relevant parties in deliberations and decisions.

2. Prepare for unexpected contingencies.

An old adage that sums up why contingency planning for your business is important: "hope for the best, prepare for the worst."

Successful business owners are often keenly aware that even the best of plans can be upended by the unexpected. Your succession planning should include contingencies for "what if" scenarios.

A plan for unanticipated leadership disruptions should prepare your company for unforeseen circumstances, such as the illness, disability, or sudden death of an owner, so that you won't be left floundering in an already stressful situation.

3. Do sweat the small stuff.

When it comes to succession planning, the minutiae – from expenses and cash flow to income replacement and taxes – can be just as important as the big picture.

Succession planning details should also, as applicable, include wills, trusts, estate plans, buy/sell agreements, and shareholder agreements. A detailed legal framework will keep everyone on the same page.

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4. Schedule structured meetings with family members.

Ensuring a smooth transition from one generation to the next requires the involvement of all the family members involved with your business. While it may be tempting to have informal talks, structured meetings can make sure that you come prepared to discuss the nitty-gritty details – including some details that may provoke strong reactions.

This process often dovetails with estate planning decisions about who will inherit your business. Part of the process should involve an objective assessment of the competencies of family members to manage the business.

In some cases, hiring a moderator can make it easier for family groups to focus on succession planning and avoid possible infighting. Moderating family business meetings sometimes requires the dispassionate involvement of a neutral third party. Your outside facilitator could be an attorney, an accountant, or a trained mediator. Professional credentials are often less important than understanding both the challenges of developing a family business succession plan and the nuances associated with a particular business and industry sector. A company's existing network of advisors and board members is often a good starting point for referrals to potential candidates.

5. Review your balance sheet and obligations.

A detailed review of your company's balance sheet and loan agreements can help ensure that you're optimizing relationships with financial institutions, and can also identify any potential roadblocks to a smooth transition.

To avoid any surprises, transition planning should include a complete inventory of current financial and accounting records, including outstanding payables and receivables. Your transition team also will need details and access to all banking and investment accounts.

Other important details include customer lists, vendors, creditors, loans from financial institutions or other investors, any outstanding tax liabilities, and any obligations to prior owners/investors (if you are not the original owner).

6. Get a preliminary valuation – and come to terms with it, if it's not what you thought.

It's essential to have a realistic understanding of your company's value in order to make informed decisions about succession options.

A qualified appraiser or accountant can help you determine the value of your business, putting a price tag on both tangible and intangible assets. Don't forget that emotions can often get wrapped up in a family business, and the valuation may differ from your or your family's expectations. Take the time now to come to terms with the professional valuation and make decisions accordingly.

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7. Consider client retention.

The long-term success of any business depends on having a stable customer base. Continuity during a business transition is essential for keeping your customers happy and retaining them once new management or ownership is in place.

Transition strategies should include plans for maintaining client relationships during a leadership change. In particular, customers will want to be reassured about continuity of service. Failing to communicate succession plans clearly with clients, employees, and other stakeholders can result in loss of current and future business, and a decline in business value.

8. Value your employees.

Customers aren't the only ones who need hand-holding during a business transition. Consider your most important employees outside of family, and how you will retain them during a transition. Skilled employees are one of your most valuable assets. A transparent succession planning process can help to keep them loyal during and after a transition.

9. Assemble a team of trusted advisors.

Succession planning requires knowledge and skill. You'll want to assemble a team of professionals who can help take your business from the analysis stage through execution of a transition. This includes seeking professional guidance from lawyers, accountants, bankers, and succession planning consultants.

Working with outside experts can help you formulate a plan independent from the potential bias of internal employees. Outside advisors also can help you formulate a strategic plan that aligns with the organizational culture of your business. This process can make it easier for families to identify qualified successors during a transition.

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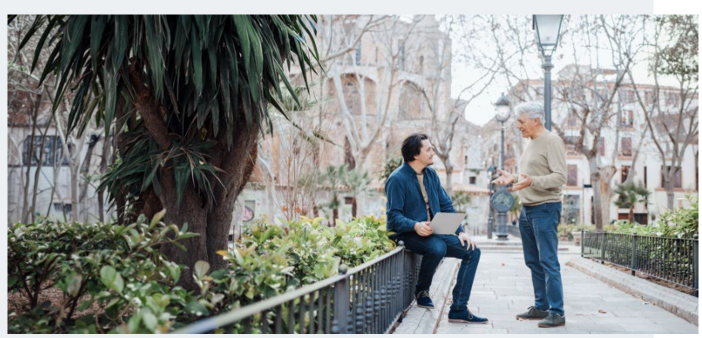

10. Avoid advisors with conflicts of interest.

Be careful about relying on any advisors, business consultants, or family members who may have a beneficial interest in your succession plan. It is important to choose advisors who prioritize your goals and the wellbeing of your business over their own financial gain. Advisors with a financial stake in a particular outcome might not provide unbiased guidance. You want to work with a team of independent experts.

Failing to plan is planning to fail.

A solid succession plan can benefit a family-owned business by setting the stage for retirement, involving key stakeholders, reducing taxes, and, perhaps most importantly, providing for your family's future harmony and prosperity.

Once your plan is in place, the last step is to make sure that it's clearly documented on paper – and to fully loop in both family and relevant staff members to avoid any confusion when it's time to actually make the transition. By following these steps, you'll be well positioned for continued success.

Learn how BMO's wealth planning professionals can assist with business advisory and succession planning.