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Building a Succession Plan

As we consult with clients regarding the transfer of a family business from one generation to the next, we often run into one of three scenarios: either the client has 1) put off planning 2) is completely paralyzed by the perception of a daunting process or 3) they have completed parts of the plan but have neither updated them nor rounded them out.

Recently, I was able to construct a Succession plan for a local construction firm, now owned 100% by 2nd generation. The owner is in his early 60s and has a strong desire to see ownership pass to two sons, who are very active in the business. He was able to purchase the business from his father and wants to lend them the same opportunity. He himself would like to wind down over time but stay engaged at some level for at least 5 years.

The process we take in these cases involves quarterbacking several players in the clients' financial and business life. Coordination with attorneys, CPAs/accountants and investment advisors is critical to achieving a successful result. The business or the "Golden Goose" is the foundation to several aspects of the business owner's life, including Retirement, Estate Planning and the Succession or sale of the business. Making sure that all advisors are on the same page, as a result, is vital.

A well thought out and well executed plan should always incorporate both:

1. ***Long Range Plan***
   a. **Retirement**: what is your vision? travel, kicking back, continuing to work part time or starting a new venture
   b. **Succession**: what is ideal or practical? sale of the business, transfer to next generation or liquidation
   c. **Estate Plan**: who gets what and when? Do you have children in the business and others are not? Is it fair to divide every asset equally, or are there other equalization techniques that would help "keep the peace"?
2. ***Contingency Plan***
   a. **What Ifs?:** Several things can interrupt a great plan and vision; either death, disability and divorce can have a devastating effect but, like most risks, can be managed
   b. **Family Income:** without the proprietor of the "Golden Goose", how will the family and employees' families be affected?
   c. **Debt:** doesn't go away because you have…who will inherit business and family obligations?

As mentioned, the cornerstone to all these components is the business itself. Business Valuation is a must. Not only does it clear the business owners' mind about what the business is worth but what would a potential buyer pay for it? What is it worth to your family without you around? What will the IRS say it's worth? How about a potential buyer? The combination of Business Valuation and a Buy/Sell agreement (reflecting the valuation) plays a huge role in any successful plan.

Our construction client was thrilled with our approach to solving his questions, concerns and long-term vision. Our creativity enables him to achieve several objectives concurrently:

- Long-term Retirement: wind down, retire in 5 years, adequate income from the business over time
- Secured his wife's financial picture through buy/sell agreement where sons will use insurance proceeds to purchase stock from her, if untimely death
- Discounting and liability leverage helps reduce make the purchase affordable for the inter-family sale of the business to the sons
- Equalization of the estate for two children not involved with the business
- Asset protection through use of trusts and pre-nuptial agreements with sons
- Savings of $400,000 in transaction costs (taxes) through creative strategies

According to the Family Business Institute and several other sources, only 12% of family businesses survive to the 3rd generation and 3% into the fourth and beyond. Study after study suggests the number one reason for failure is the lack of planning. An investment of time into your legacy by working "on" your business and not just "in" your business can yield dividends for generations to come.

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