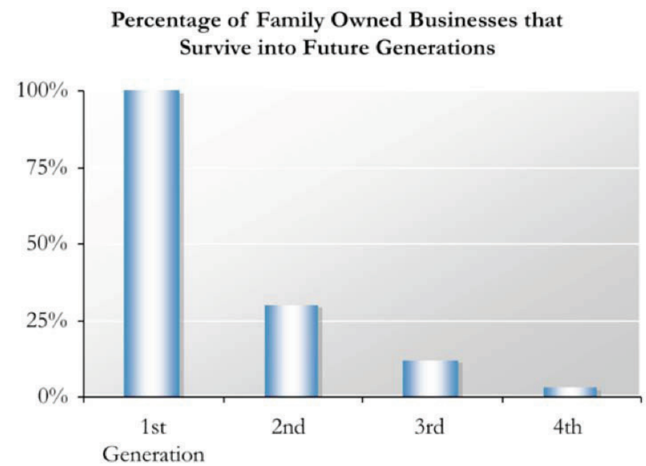
FROM OWNING TO EXITING—
MANAGING THE RISKS OF TRANSITION
IN A FAMILY OWNED BUSINESS

Family Owned Business Resources

INTRODUCTION

Statistics on the failure of family-owned businesses are well known. While more than 93 percent of businesses are family owned, only 30 percent survive in the second generation while 12 percent make it to the third. For family-owned businesses, growth strategy, succession planning, and exit strategy are laden with unique complexities. Sound solutions to these issues, formulated by impartial trusted advisors, can have significant influence on whether the business continues successfully well beyond the founder.



Addressing the unique business and relational characteristics of a family-owned company requires a team of professionals with expertise in business strategy, operational techniques as well as family systems counseling.

One of the most important aspects of any business transition is dealing with the family as a precursor to determining the optimal long-term plans for the business. Equally as important is the early participation of an objective team during the initial analysis and planning of a transition plan or exit strategy. This insures that once the strategy is formalized, the business owner, entrepreneur and his/her successors are able to take the company further, faster and on the desired course.

Family companies typically don't seek the outside expertise to navigate the business/ family landscape until spiraling disasters are rampant across the organization. Yet proper assessment and planning for transition, succession and/or exit, along with a methodology can quickly and effectively be adopted to reduce risk and greatly increase the rate at which organizations can take full advantage of the company's core competencies.

Reducing risk and harnessing a family company's essential strengths requires the creation of a growth-oriented, strategic plan, an aligned succession plan and an exit strategy that accounts for the owners' transition preferences.

CREATING A *SUCCESSION-DRIVEN* STRATEGIC PLAN

As time draws closer to an owner's exit or transition, there is renewed interest in maximizing the value of the business. Placing growth "*afterburners*" on a family-owned business is not easily accomplished. Owners often have operated and managed the business for many years with their own instincts and management style, and may not have had a well-documented plan. However, as the exit approaches, formulating a strategic plan and an immediate growth strategy are key elements to ensuring that the valuation of the business is maximized. A well-thought-out growth strategy should include all three aspects of revenue, profit and talent.

Revenue enhancement and growth are about bringing company products to new customers and new markets, and perhaps even introducing new products. These can be variations of the company's core product or completely new offerings that expand the overall customer base. It might include looking for new sources of revenue, via new distribution channels, customer segments or geographies. It should deliver opportunities that can be rolled out almost immediately, as well as major long-term revenue enhancement strategies.

Marketing and sales strategy might require a repositioning of the company, using state-of-the-art tools and techniques. Often it necessitates a deep analysis of the industry's competitive landscape. And it will need to include an online strategy; how to use the Internet to grow sales.

Perhaps the business needs reengineering of its infrastructure to be able to execute growth projections and to take advantage of economies of scale. The planning may require examining the company's processes to ensure that they deliver the highest quality goods and services, in the most productive way, at the most competitive prices.

The family succession plan is critical to the success of the strategic planning process. The leadership team needs to be aligned with the strategy. The most important ingredient of the growth strategy is who will execute the plan—the ability to execute will most certainly determine success or failure. Therefore, the succession plan must be aligned and integrated with the strategic plan because the successor will need to buy into its substance and participate in its execution.

CREATING AN *ALIGNED* SUCCESSION PLAN

Successful growth relies heavily on management execution. This imperative is particularly challenging in many family-owned businesses.

Once the growth strategy is formulated, the skills, abilities and readiness of the successor(s) must be well understood to ensure that the plan can be executed successfully. The family succession plan should include strategies to put the business interests ahead of the family interests and should emphasize merit over family position. The plans for succession need to be in alignment with the immediate and long-term vision of the company. The days of succession based on birth order are fading as companies realize that their success is tied to the knowledge, skills, abilities, passion and commitment of the successor. Whether it is succession to a senior management team including a family member, partial sale to an investor, sale to a strategic buyer or some other type of exit, family business owners need to understand how to determine the best candidates to lead the company in the immediate future and beyond.

HOW DO YOU CHOOSE A SUCCESSOR ALIGNED WITH THE COMPANY GROWTH STRATEGY?

It is extremely important to *simultaneously* develop the family succession plan and the growth strategy. One must be born from the other. They must be in synch, interdependent and based upon the knowledge, skills and abilities of the successor to successfully execute the growth plan. As the growth strategy is being formulated, and it is well understood what talent will be required to grow the business, potential successors should be assessed to determine their individual strategic alignment and fit.

Otherwise the business owner will spend a lot of time and money developing a succession plan that will almost always fail. Sometimes the failure is recognized only after the death of the owner when the "plan" is sprung on the family during the reading of the will. Often the legacy the parents were trying to create for their children and grandchildren is destroyed because of greed, misunderstandings and the lack of involvement in the family succession planning process.

Most business owners might identify the following areas as "must-have" skills for the success of their business:

- Decision-making abilities
- Leadership abilities
- Risk orientation
- Interpersonal skills
- Temperament under stress

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Descriptive And Predictive Assessment Tools

Is there a way to objectively assess with predictive accuracy which successor candidate will demonstrate proficiency in these skill areas? More and more family-owned businesses are turning to descriptive and predictive assessment tools to find these answers. These tools are not new.

Simply put, assessments have been helping companies make better hires for several decades. Family-owned businesses face many challenges and considerations as owners consider transition and succession plans. Proven descriptive and prescriptive assessment tools provide a rational basis for creating a succession candidate pool. If parents decide that their heir or heirs are the candidates to be considered, these tools can provide a useful benchmark for their development.

THE EXIT STRATEGY: CASHING IN DOES NOT MEAN SELLING OUT

There has been and will continue to be a huge jump in the number of owners that want to exit their businesses due to baby boomers retiring. The exit strategy is a process that should be highly customized for each business; it involves the design and implementation of an owner's successful exit from his or her business. Exit strategies take into consideration the owner's unique personal objectives to convert their current business into the desired outcomes. The exit strategy helps to maximize the financial return, minimize the tax liability, plan for contingencies and increase the likelihood of a successful transition of the business.

Each business owner's unique objectives drive the creation of their exit plan. The first step in the process is to articulate the owner's objectives so that the exit plan focuses on achieving those goals. Key exit objectives identified as part of the exit planning process include:

1. The planned or desired departure date;

2. The value that the owner wants or needs from the business, and;

3. The individuals or entities to which the owner wants to sell/transition/transfer the business.

Determining the current valuation, what the business is worth, and how much cash the business generates, are essential pieces of information necessary for planning a successful exit. In addition, the owner's current assets and income that are not connected to the business are included in the analysis. Finally, both of these are input to determining the alternative and optimal paths towards the realization of the owner's objectives.

The creation of an immediate growth strategy to protect and build upon the value of the business is paramount to ensuring that there is a clear path towards a successful transition/exit. A detailed plan for how to retain the current value while creating future growth should be developed by the firm's advisors.

Early on, owners will need to decide to whom transfer of ownership in the business will go. For those who want to sell to outside parties, the value proposition and ultimate valuation of the business will depend upon the target buyer(s) and how well the company can be positioned with those buyers. For those who wish to sell to insiders, a detailed plan should be developed to transfer the business to children, key employees or co-owners as appropriate. It is important to build a risk profile for the business so that any unforeseen events that change the plan can be mitigated so the owner may still achieve his/her objectives.

Finally, personal wealth and estate planning must be incorporated into the plan. This aspect will allow the owner to preserve his/her wealth but minimize taxes using lifetime and estate planning methods.

THE ALL IMPORTANT TRANSITION ADVISORY TEAM

Family business owners who want to take full advantage of the sacrifices they have made in creating a successful business are in the position to gain a significant return on their investment with the right exit strategy. It is the last important decision an owner will need to make. However, there are a number and types of advisors that you will need to help you work through the exit / transition planning process. It is also important to ensure that the advisors you have retained to assist you with the operation of your business, are qualified and have sufficient experience to be part of this advisory team. Most of the advisors you will need will come from outside independent professionals who specialize in each area and who are unrelated to others retained by you. Researching and retaining advisors, who have experience working as part of a team orchestrating exits for their business owner clients, will help you quantify and attain realistic exit objectives.

The types of activities that are necessary to successfully exit the business include:

- Setting realistic objectives
- Determining the sale price you are likely to get for the company
- Maximize growth in the short term by creating a growth strategy and helping to execute the plan
- Working with potential buyers by collaborating as to how they might leverage the firm
- Minimizing the tax implications of the sale proceeds
- Designing and implementing plans for the transfer of wealth to subsequent generations
- Providing advice and counsel as to when is the best time to sell or transition the company

ABOUT FAMILY OWNED BUSINESS RESOURCES (FOBR)

Family Owned Business Resources is a portal to and for the world of family owned business. It is a site that offers useful tools and resources at a modest price point to people who own, work in and are around family business. The people who work here have been practitioners working with family owned businesses for fifteen years. During that time we have learned a lot and come to have great respect for the owners, operators and governors of family owned businesses. We would like to share with you what we have learned and help you be even more successful than you are today.

Our Mission:

- Our mission is to provide best in class information, products, and services to the family owned business stakeholder community. Our team brings a deep understanding based upon years of experience as practitioners in the field of family business advising.

Our Vision

- FOBR is the resource of choice for rigorous, affordable and relevant information critical to the success of family owned businesses.

Our Core Values

- Our commitment is to enable family owned businesses to flourish beyond three generations, by using seventh generation thinking.
- We are ethical: We maintain high ethical standards in the conduct of business.
- We are accountable: We are accountable for the quality of our resources, the responsible dissemination of the resources we have developed.
- We are constructive: We will be selective in the information we disseminate, ensuring that it is constructive and additive to the family business community.
- We are collaborative: We work collaboratively, seeking the input of those who are affected by our work, internally and externally, and partner with like-minded groups to achieve our mission

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