The Perplexing Mystery of Succession Planning

By Mike Henning

Not long ago, a reporter asked me several excellent probing questions about succession planning. The purpose of the questions was to clear up the confusing and mysterious aura surrounding the topic of succession. Read on to see if we fulfilled those expectations.

1. *Where do you begin when preparing a succession plan?*

Because we define succession planning (generational transition) as a "cradle-to-grave" process with emphasis and energy increased and decreased during certain periods of people's lives, it really depends on where the business-owning family is in the cycle and process of their planning. Following are some examples.

Family Meeting. The family must come together and decide whether continuity of the family business is really in their best interest. Can individuals handle the stress of a business and working together with siblings, cousins, and parents? Are members of the next generation cut out for the job? We find that most parents assume their children, or at least one of them, will want to take over the family "gold mine." Thus, this meeting to discuss the future of the business is often overlooked, and the owners proceed as if the business will remain with the family through another generation, which may not be true. If not, the parents are surprised and dismayed. Yet, they have never asked their children about their career intentions.

Goal Setting. The family should draw up a statement of shared goals, including a vision of how they will function in the years ahead when the parents are uninvolved in the family business operations. Once again, this step is often overlooked during the process. Yet, without a common vision and set of shared goals, the junior generation is commonly characterized as overly ambitious when it comes to spending money that is not theirs to spend. This situation can easily become a succession stopping point, and parents often make remarks like, "Our kids are trying to spend our inheritance" or "The kid has no sense of the value of a dollar so how could we let him/her take over the family business."

Estate Planning. Members of both generations need an estate plan, quite distinct from the management succession plan and more comprehensive than simply who inherits the business. When addressing the estate planning process with attorneys, business owners are putting their "death plan" in place and getting it aligned according to the goals, ambitions, and ideas of fairness for their children and grandchildren. The plan really states what will happen to assets and things in the event of death. It is a death plan or "what-happens-after-I-die" plan. Many people look to formulate this plan long before they know who is committed to the business and who will make careers elsewhere. Thus, it becomes very difficult to achieve accuracy within the document if you don't know who is on the bus and who may have other dreams to fulfill.

Generational Differences. Are there discrepancies in the way the current generation runs the business and how the next generation may run it? Many family businesses need to evolve from "family-first" type companies to "business-first" organizations. In a family-first company, decisions are driven by the need to solve family needs first while the company's needs come second.

Focus on Style. Many companies also need to change from an entrepreneurial management style to a more professional style. That doesn't mean becoming a bureaucracy; it means staying focused, fast, and entrepreneurial while pushing decision-making and accountabilities down into the organization. The skills required for the next president may be quite different from what has worked for the current one.

Leadership and Management. Is there a shared vision for the business? If so, who in the next generation possesses the passion and competence to implement it? Should the next generation let non-family run the company? What kinds of incentives will be needed in a private company to attract and retain top people? How much time does the current president spend consciously cultivatng leadership? If he or she spends less than 20 percent, there's a problem. Does the next generation of owners enjoy the trust and respect of the company's key long-term managers? Have successors developed the strategic thinking skills needed to succeed in the future? One thing is certain, future leaders will spend more time on communication and relationship issues than in the past.

Ownership Models. As companies evolve, they may use an owner-investor model, in which ownership is held in family entities such as family limited partnerships (for C corporations) or trusts (to hold S corporation stock). The company may hire non-family to run the business while the family pursues different career paths but retains ownership.

Understanding ownership options is important because many family businesses follow historical precedents ("This is the way Dad did it") in their planning instead of thinking strategically. Having patient family members leave their equity in the business is one way to build capital.

2. Who should the business owner consult first?

We suggest the first contact about beginning a serious generational transition plan is with one's spouse. Next would be the family, possibly a trusted peer who has been through the succession process, family business advisor, CPA, attorney, estate planner, etc.

3. What distinguishes a good succession plan from a great one? What are the essentials?

Good versus great is measured by the outcome. As advisors, we work to determine where a family is in regard to the succession process, then begin our work at that point. We identify the values of the families involved, help them set goals, teach the finer points of stretching that is involved with serious change, then put accountability mechanisms in place to make sure the plan is followed. If we can align the family's values with the goals, chances are the plan will be implemented.

The outcome of a great plan results in seeing each family member develop their talents fully and capably during their career in the family business. It sees the family itself coming closer together as individuals to support each other, become good communicators, utilize excellent teamwork both inside and outside of business, and achieve a new level of unity and harmony. They come to respect each other for who they are as individuals, and each one realizes they are better off because they are in business with the other one(s). The great plan realizes the business achieving new heights and goals never before thought possible. (For example, 25 percent increases in revenues within two years or adding 2 percent to the bottom line.) Finally, the great plan finds all family members proud of their life career choice, whether in or outside the family business, with the full support of their parents and siblings. Thus, no one family member is lost due to conflict or serious disagreement.

4. What are the consequences of not having a good succession plan?

The consequences of not having a good succession plan are clear in the poor success/failure rates in the U. S. and other countries. These businesses are often purchased by competitors or suppliers for heavily discounted prices or sold at auction, or they just quietly go out of business. This is the dark side of family business, and it often sees the virtues of passion, commitment, sacrifice, and other intense feelings for the business turn into

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vices. The media often cover stories that remind us that power, greed, money, and infighting among members of any family can and will bring the business to its knees. Almost 70 percent of private companies do not survive into the second generation.

We often see aging companies in aging industries that need change and regeneration, but aging owners are often reluctant to implement the needed actions. Thus, their passionate attachment and resistance to planned change often explains their reluctance to develop well thought-out succession plans.

5. How much can one expect to invest in the plan?

Depending on where we find the family in the process, the range of investment can be from as low as $10,000 to more than $100,000. Trying to answer this question is similar to asking a doctor how much it will cost to cure an illness.

6. How often should a succession plan be reviewed?

We often recommend that the owning family put formal structures in place to review the process and its results on a regular basis. This means that once per quarter during a scheduled meeting of a decision-making board, certain issues regarding succession planning will be reviewed.

How did we do? Hopefully we said something that helped you begin to put the pieces of your succession-planning puzzle together or put the final touches on a plan that has been under construction for some time.

This article first appeared in Mike Henning's Family Firm Advisor newsletter. For more information about receiving the newsletter, visit www.mikehenning.com, email hfbc@mikehenning.com, or call (217) 342-3728. Henning is an internationally respected consultant and speaker on family business issues.