

IN THE NEWS**Pandemic creates 'sense of urgency' for succession planning**

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Amid its many strains on companies, the COVID-19 pandemic appears to have prompted more owners to think about the future and eventually pass a family business down to the next generation.

That's according to a recent survey by the Family Business Alliance in Grand Rapids, which found that 20 percent of its 166 member companies are now implementing a succession plan and have been actively involved in transitioning leadership over the past two and a half years.

Family Business Alliance Director Robin Burns believes the pandemic has contributed to creating "more of a sense of urgency" to succession planning from one generation to another. The Family Business Alliance hosted a three-part workshop this year on succession planning that drew representatives from 24 family businesses that are "beginning to pass the baton" over a multi-year period.

As well, advisers whom the Family Business Alliance works with report that "they have been very busy with succession planning as well," Burns said.

"The pandemic has actively brought succession planning to the forefront," she said.

Still, despite more focus and understanding today about the need for succession planning, many family-owned businesses are not engaged in that process.

A 2021 PricewaterhouseCoopers survey found that just 34 percent of family businesses nationally have a "robust, documented and communicated succession plan in place."

"And, while most family business leaders have at least an informal succession plan in place, only a minority have fully embraced the need to not only have a plan, but to document it and effectively communicate it to all essential parties," according to the survey.

'Critically important'

Succession planning often represents the "biggest struggle" for family-owned business, said Patricia Soldano, president of the Washington, D.C.-based advocacy group Family Enterprise USA. Soldano said the relatively low rate of family businesses that are actively planning succession from one generation to the next is "disappointing." She urges advisers to regularly remind their family business clients that "it's critically important to do succession

planning for your business because it's not going to sustain itself if they don't do it."

"(Owners) really say that they think their business is a legacy for their children and give us that data all of the time, and yet when we ask them if they have actually given up control or partial control of your business, only 29 percent have actually done that," Soldano said, citing Family Enterprise data.

"So they may give up some of the assets or they may give up some of the ownership, but they've all struggled with: 'I don't know if I'm ready to leave,' 'I don't know if my kid's ready to take over,' 'I don't think the market's right,' 'I'm not sure the conditions are good.' Some of that is just excuses," she said. "All of the research around family businesses has proven that each generation that takes over brings in new innovation and those are the ones that survive. In today's world that changes so quickly, you need that innovation that comes from the next generation."

In its 2021 report, PricewaterhouseCoopers noted that "those businesses that have not yet begun planning for succession could be vulnerable to significant risks – risks such as fractured family relationships, a successor who doesn't have the capability or credibility to lead and reluctance from external stakeholders, who may not want to work with an organization that isn't governed by a good succession plan."

Quite often the lack of a succession plan results from leadership focused on the day-to-day operations of running the business, Burns said. The challenges of the pandemic and the talent shortage that "push them back into the field" also contribute to the lack of succession planning at many family businesses, she added.

Getting started

Family-owned businesses that have yet to craft a formal succession plan can begin by first identifying who in the family can eventually take over and whether they are "ready, willing and able" to operate the company, said Brooks Kindel, a consultant at the Michigan Small Business Development Center at Grand Valley State University who works with companies on exit planning and leadership issues.

Owners should "take the blood relationships out of it and be a little more objective" when assessing whether the next generation is capable of successfully leading the company, Kindel said.

"I see a lot of situations where the owner thinks by osmosis their son or daughter is going to take over the business. You really need to take a step back and say, 'OK, this really is just a non-related employee. Can they thrive in the position? Do they get the business? Do they have the skills and experience necessary?'" Kindel said. "The plan is getting your business ready for a transition in ownership. That's going to happen someday, somehow, and whether it's to a second generation or to a third party, either way you're doing the right thing for the business by having an exit plan. If it's a family thing, then you want to make sure that just because it's family you're not overlooking the obvious things about knowledge, expertise, skills, talent, passion. All of those things."

Two-thirds of family-owned businesses nationally have a next generation member working in the business who is expected to become majority shareholders within five years, according to PricewaterhouseCoopers.

Once the next generation has been identified, the present leadership needs to plan for the next generation over a period of years to become involved in every aspect of the company's operations, Kindel said. When it comes time to execute the transition, they need to structure the transaction so the next generation can afford it, he said.

"Provide your child the opportunity to really learn the business A to Z, and then make sure the financial end of the transaction makes sense for both the older generation and the newer generation," Kindel said. "Is there a way that it can be structured so it doesn't provide financial hardship?"

Kindel recommends that the family business early on have a valuation done that establishes a financial benchmark so the next generation understands what it takes financially to acquire the business. Kindel describes a situation involving a client where the son was going to take over the business from his father and uncle. He backed out when he concluded that he could not afford the transaction following a valuation, Kindel said.

As the heads of the family business begin to consider succession and formulate a plan, they need to start well in advance of their exit to prepare the business for a transition. Kindel recommends starting planning three to seven years prior to an exit.

The present leaders also need to think about what they'll do once they are no longer running the business and how much they need financially to maintain their lifestyle, he said. The process should include working with estate, tax and financial planners to minimize their tax obligation "because you don't want to give Uncle Sam any more money than necessary," Kindel said.

Like Burns at the Family Business Alliance, Kindel believes more family business owners are beginning to think about succession planning coming out of the pandemic.

"If there's anything we've learned the last few years, you never know what's around the corner," he said. "There's also an element of, 'OK, we survived the recession in 2008. Then we had a pandemic. I'm tired. I don't want to do this anymore.'"

A key to the planning process is the willingness of the present generation leading a company to actually prepare to step aside once the next generation is ready to take over.

That's particularly true in companies led by the founder as they transition out and hand operations over to a new generation, Burns said.

"The previous generation needs to be ready to walk away. That is the other challenge in succession," she said. "In a first-generation scenario, this is their identity, this is their legacy, and it is difficult to understand that the next generation may have a different way of running that business and it would be difficult to let that go."