

## Succession – a major challenge for baby boomers....

By Ben Cameron, Director, Bentleys

Ben Cameron from Bentleys Chartered Accountants offers some well-established advice on succession for family businesses.

In the past I have deliberately tried not to write about succession, given it has been the hot topic on every advisor's lips for a long time. However it is becoming such a large part of my work nowadays that I have finally succumbed and will share my views on this important and crucial element of the business cycle.

The statistics on small business succession are mind boggling:

- in 2010 the oldest baby boomer retires
- average age of business owners is 58
- there are 1.9 million owner-managers of businesses, with an aggregate value of \$1.6 trillion
- 30% of business owners plan to retire in the next 1-3 years and a further 27% within 4-6 years

However, here is the catch:

- only 24% of business owners have succession plans
- only 38% of business owners have identified successors
- more than 50% need their business to fund their retirement
- less than 30% expect succession to be easy!

"Succession" occurs when a person (or persons), is replaced by one (or more) others. It represents a major, once in a generation change, and has profound effects on individuals, families and their businesses. Succession can be a "crisis response" to a major catalyst - such as an accident or heart attack. This is the worst of all situations as major challenges have then to be faced at a time of maximum vulnerability.

Ideally, succession should be a planned, structured and controlled process to maximise the positives and to minimise the negatives to the business, to the family and to the individuals most concerned. The process requires time, in an ideal world – up to seven years or more.

Having this kind of lead time enables the business to demonstrate to its external stakeholders that the transition will be seamless. It allows the outgoing leader to ensure that they are adequately prepared for retirement (or whatever stepping back or stepping down means to them) - both in terms of their mental state and their financial arrangements.

### **Succession Options**

There are primarily five ways in which succession can occur:

#### *Succession by Family Members*

Selling to a family member is the preferred option for around 50% of all family business owners, but it only actually happens for less than two-thirds of this group – even when they try to give it away to another family member.

#### *Partial/Total Management Buyout/Buy-in by Staff*

If the family won't or can't take over the business, the next preferred option is to see it passing into the hands of employees.

*Sale on Open or Restricted Markets - Trade Sale, Capital Raising, IPO etc*  
This option requires dedicated accounting preparation, presentation, and negotiation well in advance of the planned hand over date to ensure that value of the business is maximised.

*Merger, Acquisition or Alliance to Friends or Competitors*

Handing over the reins to others inside or outside the industry can be an option for some businesses.

*Liquidation*

Transferring or breaking up the business to sell its assets is usually the least desirable option as it denies the outgoing leader the opportunity to get a return on the goodwill they have developed in the business over the years. (For rural properties there is no goodwill element so this is less of a concern for them). It also means the demise of the business. This can be a major emotional wrench for someone who sees their life's work going down the drain.

However, for families that are poorly prepared for succession, or where there are significant tensions and conflicts in the family, this can provide a less-stressful way of "divvy-ing" up the business by distributing proceeds, rather than responsibilities, to the family.

**10 Golden Rules for Succession**

**DO:**

1. Do make succession a process, not an event. Do it over time and according to a plan.
2. Do be professional, not protectionist. Remember that business is business and family is family. Each can readily support the other, but there is a profound difference between the two. The sentimental choice of successor for family reasons must also stand up as the rational choice for business reasons.
3. Do appoint the best steward for the business.
4. Do acknowledge that there are always other 'options'. Families have a tendency to be rather "one-eyed" when it comes to succession and business ownership issues. For example, a remarkably common solution is to choose the eldest son as the successor, irrespective of the desire or fitness of the firstborn for the role. There have been many forced attempts at succession that, to external eyes, were doomed to failure from the start. Failing to look at succession strategically can leave otherwise very canny businesspeople completely blind to impending disaster.
5. Do establish "how much is enough?". For reasons that seem incomprehensible to outsiders, some business owners appear to feel they must demand a full commercial price for their interest in the business when they sell to family successors, even though they don't need the money for their own financial security. This is usually dressed up (self-justified) as some sort of motivator to "inspire" the successor to have the same "hunger" they believe they themselves had many years earlier. In reality, all it does is saddle the successor, and/or the business, with a level of debt that they usually can't afford to bear and therefore becomes a major source of stress and a common reason for throwing in the towel after a couple of years. For some ex-leaders, this even allows them to demonstrate their indispensability, and invulnerability, through a "second coming" - when they ride in to the rescue of the business and the family.

If the family business is to be a treasure to the family, rather than a burden, as much of it as is possible should ultimately be gifted back into the family. Normal commercial reasoning, and weak egos, have no place in this equation.

6. Do respond to the outgoing leaders "fear of the abyss". For many business owners, their business has been their life. Although they may not put it in these terms, sub-consciously they fear that not being in the business may be their death - perhaps even literally. Some proprietors get very excited about implementing the whole succession process and talk the talk with complete confidence, yet when it comes to actually prising their hands off the reins, muscle spasm can set in, they choke and they can't let go. This can be highly distressing for everyone. I find that the main indicator is whether or not the said proprietor has "got another rock to hop to".

**DON'T:**

7. Don't try to clone the current leader.
8. Don't demand 60 year old behaviour from 30 year old candidates. Just as parents cannot realistically expect their small children to act with the experience that comes with adulthood, so an outgoing proprietor should not judge their successors by what they believe they would do under the same circumstances. A proper assessment of worthiness has more to do with whether the job gets done as required, rather than the style with which it is done. This can become a trap where a reluctant retiree finds faults where none really exist.
9. Don't hand over the reins until you are ready to get off the horse. Some family businesses place the next generation on trainer wheels, and then load them up with responsibilities without providing any real sense of ownership as a counter-balance.
10. Don't sacrifice business, family and personal objectives just for tax and wealth benefits. This is in keeping with the earlier point regarding "how much is enough". Of course tax issues are important, and nobody likes to pay more than they must, but during the succession process there are more important values at stake. The key objective should be to ensure the smooth transition of the business from one generation to the next, which allows smooth transition of both the entering and outgoing parties into their new roles in life.

Planning and pacing the succession of your business will make a world of difference to both yours and your successor's future.

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