

# A Comprehensive Succession Plan Can Help Your Business Endure

by Kevin Spafford

Family businesses account for 80 to 90% of all business enterprises in North America<sup>1</sup>, and provide 60% of U.S. employment, 78% of all new jobs, and 65% of all wages paid<sup>2</sup>. But essentially all of these businesses will lose their primary owner by death or retirement by the middle of this century. Most commercial farms in the U.S. today are family-based businesses.

“They can call it asset, I call it an anchor,” said a retiring farm business owner as we started the consultation. His son was going to manage the parts department and his daughter was going to become the general manager of this family owned tractor dealership. The operation was established by his father years before, and now he was planning to transition the ownership to a third generation.

The situation is not unique—in his 42 years at the helm this owner reinvested every available dollar back into the business. Now he realizes that there may not be enough money to fund a 20 to 30 year retirement. He is faced with a severe money shortage and the less than desirable alternative of drawing equity from the business or asking the children to buy their respective shares.

For the business owner, retirement is a light at the end of the tunnel. For some it is a sense of freedom and reward; for others it is an oncoming locomotive at full speed. A business is only as valuable as the return a person is able to derive from ownership.

## The Background

Comprehensive succession planning may be the most critical issue facing the American economy over the next few decades. The creators/controllers of this wealth must decide how to best pass their ownership interests to subsequent generations while still trying to perpetuate these entities. Equity may easily constitute more than 90% of a family’s financial security, retirement nest egg, and potential legacy. Yet past statistics demonstrate that only about 30% will pass to a second generation, less than 10% will pass to a third, and about 4% will go to a fourth.<sup>3</sup> The three leading causes of failure to transition to the next generation are:

- 1) Inadequate estate planning
- 2) Insufficient capitalization
- 3) Failure to prepare the next generation

All of this leads to a growing demand for better planning, integrated training systems, more carefully administered business issues, and the responsibility to think, act, and operate in a more formal business-like fashion. From the threats distressing farmers and agribusiness owners alike, there is no escaping the passage of progress. Threats from outside, shrinking pools of skilled employees, administrative pressures brought by legislation, and constant consolidation did not happen overnight.

## The Succession Solution

A comprehensive succession plan will address the *needs of the family*, the *desire of the owner*, and the *demands of the business*. It is a healthy progression in the life of a viable family enterprise. It is the current owner connecting the past and the present to the future through a process of planned transition. It is built on the framework of the following five disciplines:



A **dynamic business plan** is designed to maximize the profit and equity returns from business operations. It is a complete review of the systems of production, the products/services offered, and the resulting streams of income. It details growth/development/expansion, explores tangible/intangible product opportunities, and designs an area of specialization.

An **ownership transfer/leadership development system** is the process of deciding the most advantageous method of ownership transfer, and implementing a system intended to teach and reinforce the skills of leadership. Being an owner means being a leader, and leadership is about the people you develop and the systems you install for continuing success. Most owners need to design a path to instruct and inspire next generation management.

**Wealth creation/capital management** will build a reservoir of financial resources to use as reinforcement through the storms of transition, a learning tool for judiciously managing money, and a reserve for the uncertainties of the business cycle. Money management seems to be the bane of every family owned business. Solve the cash flow problems of a business and many issues become minor irritations rather than make or break decisions.

A fully funded **retirement option design** is paramount to a successful transition plan. Many owners do not, or will not retire due to an unstated lack of preparedness. Most owners are not interested in imminent retirement. When asked about retirement, owners scoff and respond with something about, “enjoying work and not knowing what else to do...” An option date lends urgency to this important objective.

Finally, an **estate plan** acts to minimize the estate tax and transfer obligations while planning for an equitable distribution of assets. Planning is required to address spousal support, and to lend peace of mind for addressing the potential of dying too soon. History shows that those most threatened by change are the least prepared. I am a firm believer that success is of our own creation. Succession planning is a healthy progression in the life of a viable family enterprise. It is the current owner connecting the past and the present to the future through a process of planned transition.

## STEPS FOR SUCCESSION PLANNING

### Dynamic Business Model

- Brings your vision to life
- Specifies goals and action plans
- Maximizes income, equity appreciation, and personal satisfaction

### Ownership Transfer / Leadership Development System

- Establishes leadership curriculum
- Matches skill development with business needs
- Develops a ‘bench’ of successor candidates

### Wealth Creation / Capital Management

- Diversifies financial base
- Reinforces sound money management
- Ensures financial fortitude

### Retirement Option Design

- Promotes preparedness
- Ensures a healthy long-term standard of living
- Allows retirement without jeopardizing business stability

### Estate Planning

- Minimizes estate tax and transfer obligations
- Provides for spousal support
- Addresses contingency concerns



## For More Information

Links to additional succession planning information may be found on Kevin Spafford's website: [www.Legacy-by-Design.com](http://www.Legacy-by-Design.com) (see the list of resources in right-hand column on the 'Coffee Shop' page of the website).

## The Writer

Kevin Spafford, founder of Legacy by Design, is a *Farm Journal* columnist ("Succession Solutions"), and author of Legacy by Design: Succession Planning for Agribusiness Owners (Marketplace Books, 2006). Among his 2007 speaking engagements will be a presentation at this year's Top Farmer Crop Workshop.

- 
1. *Family Business Review*, Summer 1996
  2. *Financial Planning*, November 1999
  3. Family Firm Institute (Joseph Astrachan, Ph.D., editor, *Family Business Review*)

## Questions to Ask Yourself:

1. Do I have an interest in continuing to develop my business for:
  - Profitability to support expansion?
  - Maximum valuation for sale?
  - As a legacy to future generations?
2. Which of these offers more appeal:
  - Growth and development?
  - Sell and walk away?
  - Acquiesce to diminishing returns?
3. Do the participants of this business possess the entrepreneurial spirit, energy, and enthusiasm to create something bigger than the sum of the parts?
4. What role does the business play in my family life?
5. Are my children, grandchildren, loyal employees and/or extended family interested in continuing to grow the business?

