

How to Plan for a Successful Succession

Richard Eisenberg (NextAvenue, MarketWatch)

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Nothing succeeds like success, the saying goes. But for family businesses, it's smart family business succession planning that can be the key to sustaining the company in the future and keeping it flourishing. Problem is: few family business owners are doing a good job preparing to turn their enterprises over to the next generation.

"Succession planning is a difficult thing because it's tied up with the hard-to-face fact that the owner is going to retire," said Ritch Sorenson, Opus endowed chair in family business and academic director at University of St. Thomas in Minneapolis. "No matter how accomplished the children are, there may be questions about whether they can take over and run the business as well as the parents have done." (The new website [Familybusiness.org](http://familybusiness.org)(<http://familybusiness.org/>) is an offshoot of the University of St. Thomas' Entrepreneur and Innovation Exchange — eix.org. Full disclosure: The Schulze Foundation, which funds EIX, is also a funder of Next Avenue.)

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Succession Planning: A 'Perennial Problem'

Succession planning "is a perennial problem for family businesses," a 2017 report from PwC, called *The Missing Middle: Bridging the Strategy Gap in U.S. Family Firms*, said.

In fact, the 2016 Family Business Survey by the National Bureau of Economic Research Family Business Alliance found that 43 percent of family-owned businesses don't have a succession plan. Yet roughly three quarters of the enterprises plan to pass ownership to the next generation.

"Generally, most family business owners find themselves so involved in the day-to-day operations, they're not thinking of what's next for them personally or for their family and how that intersects with the business," said David Neubert, managing director of SunTrust Business Transition Advisory Group.

The Irony for Family Business Owners

It's ironic, notes Joe Fahey, PNC director of business succession planning, "that the things that make these owners successful — vision, communication and execution — are things they need some coaching on to apply those skills for the family's strategic plan and vision."

Without proper succession planning, the business and the family can wind up having heated disagreements and legal tangles— sometimes played out in the local media. "The worst case scenario is the future owners become embroiled in a conflict that escalates publicly," said Sorenson. Added Fahey: "The only winners from fighting are lawyers and the IRS."

Start Succession Planning Early

If you're a family business owner expecting that one or more of your children will take over the venture at some point, the earlier you can start planning for that transition, the better.

"The rule of thumb we have found is that you need at least ten years to plan for succession," said Sorenson. "There are a lot of things you have to work through." They include estate planning, taxes, liability, ownership stakes and voting rights.

Long-term succession planning can give your child or children time to learn the management tasks and for you to see how well they're executed. Fahey said you might tell your child: "I will set up a board of advisers that I will be on and we'll see how you do. You'll have nonvoting

shares, and to the extent you can prove you can run the company well, when you pay off the nonvoting shares, you can then buy the voting shares.”

The longer the succession planning process, said Neubert, “the better your chance to mentor [your child or children] and bring them along to see if they can step up.”

Which Child or Children Will Take Over?

The most important thing to work through, of course, is determining which child or children will run the business and when that will happen. Those decisions can be fraught for families.

“It can be emotional,” said Neubert. “It has implications for the business itself, financially, and impacts the legacy of not only what you want the business to look like over the long term, but how it intersects with your family and the community.”

Some owners mistakenly assume a specific child can take over the business when the reality is the son or daughter lacks the appropriate experience and expertise. “That can be a disaster,” said Sorenson.

Diminishing Interest by Younger Generations

One challenge is that fewer members of the younger generation these days are interested in working in the family business, let alone ultimately running it. Just half of the family firms PwC surveyed said that successors to key roles will be family members.

According to PwC’s 2016 survey of family businesses, of those expecting to change ownership in the next five years, only 52 percent of them plan to keep the ventures in the family, down from 74 percent in its 2014 survey and the lowest number since 2010. Of the family businesses expecting to change ownership more than five years in the future, just 69 percent plan to keep the companies in the family, compared with 79 percent in the previous survey.

Working With a Family Business Adviser

Assuming one or more of your children are interested in owning and running your family business, you’ll likely

want to work with a family business adviser to help make the succession smooth.

“We encourage clients to let advisers help with strategic positioning and shine a light down the road,” said Fahey.

The adviser can objectively discuss with you the pros and cons of handing over the reins to one or more of your children versus bringing in an outsider to run the company — so-called “hired gun” management.

A family business adviser can also be especially helpful in working with you to draw up necessary succession documents. Just 23 percent of family firms have a “robust, documented plan,” according to PwC.

“The vast majority of family business owners have no clue that there are well-established governance processes to help prepare for succession or how to find them,” said Sorenson. “But there are numerous books and lots of consultants who can help.”

Sorenson recommends preparing two kinds of documents: a charter ownership (with agreements on what it means to be the owner of the business) and a constitution. You’ll want to do this with help from lawyers and often insurance agents, noted Sorenson.

Letting the New Owner Take Over

Once you do hand over the company to your child or children, allow your new owner or owners to run the show.

“The senior generation needs to let the next generation make some mistakes and learn from them and do things differently,” said Neubert. “Sometimes, that’s challenging.”

Richard Eisenberg is the Senior Web Editor of the Money & Security and Work & Purpose channels of Next Avenue and Managing Editor for the site. He is the author of How to Avoid a Mid-Life Financial Crisis and has been a personal finance editor at Money, Yahoo, Good Housekeeping, and CBS MoneyWatch. @richeis315
(<https://twitter.com/@richeis315>)

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