

Pass It On, Inc.

Issue 26

Planning to Keep Families in Business

Since 1947

SURVIVAL KIT—Risks of a family-owned business

Reprinted from an article in the Colorado Springs Business Journal. Written by Don See.



ONE OF THE STRENGTHS OF A FAMILY-OWNED BUSINESS is often the simplicity of management structure. A relatively small group of individuals, sometimes one key owner/manager, makes the critical decisions that make the company run. This allows for speedy adjustment to changes in the marketplace and avoids the delays and confusion that often accompany more complicated, multi-level management. It also exposes the company to a serious risk—the loss of a key person through sickness, accident or death.

This reality was revealed in a study done several years ago, which concluded that nearly two-thirds of closely-held companies failed to survive the death or extended disability of a key owner/manager. Within two years of the loss of that key individual, over 60 percent of the companies were no longer in business. Some were sold, most were liquidated.

The best way to avoid this unfortunate outcome is for the company to prepare ahead of time. Two specific actions are recommended for every business owner:

1. Develop and Inform Key Employees.

There is real temptation for a business owner to keep the critical information about the company secret. Key contact with customers, suppliers, pricing guidelines and general decision-making is never shared. This creates an atmosphere of ignorance and uncertainty if the owner is unavailable for an extended period. It is far better to bring key employees into the loop and give them the information and permission to participate in key decisions affecting the company's future and success.

2. Prepare a Survival Kit.

The owner should write down relevant information in case anything happens. We encourage the owner to use the "Business Continuation Plan Outline" worksheet to prepare instructions for the employees and the family. The worksheet can be found on our website: www.passitoninc.com. Advise them as to the best approach to take to complete the work-in-progress of the business, and to decide on the best direction for the company. This provides crucial information that will be needed to deal with customers, bankers, suppliers and employees. This outline is provided as an aid, and different businesses will have different issues to address. This applies to professionals in practices as well as operating companies.

There are other strategies that can guarantee the survival of a family-owned company that we'll share in a future article. For now, improve your company's chance if anything happens to you by providing a survival kit.

Don See, president of Pass It On, Inc., has a national clientele of family-owned businesses, providing them with succession and estate planning assistance. He can be reached at don@passitoninc.com.

BUSINESS CONTINUATION PLAN OUTLINE

"If it could go the way I want it to, how should it go?"

Questions-Which Apply?

1. MANAGEMENT DECISIONS

- ☐ A. Who takes over as **CEO, Managing Director**?
- ☐ B. Should there be incentives to **Retain Key Employees**?
- ☐ C. Should there be an **Interim Board of Directors**? Who?
- ☐ D. How does the company complete **Work In Progress**?
- ☐ E. Do you want **Severance, Transition Pay for Employees**?

2. FINANCIAL DECISIONS

- ☐ A. Who assumes or pays the **Personal Debt Guarantee**?
- ☐ B. When do you pass on critical **Bank Relationships**?
- ☐ C. Who needs **Key Person Life Insurance**?
- ☐ D. Who takes **Control of Receivables, Payables**?
- ☐ E. Who maintains **Patient, Client Files**?

3. DIRECTION OF COMPANY - Strategic Plan

- ☐ A. Is it best to **Maintain Under Family Management**?
- ☐ B. Is it best to **Maintain Under Employee Management**?
- ☐ C. Should the family seek an **Outside, Qualified Buyer**?
- ☐ D. Can it be **Preserved for Young or Non-involved Children**?
- ☐ E. Is it best to **Wind Up Business, Liquidate**? When?

4. DISPOSITION OF COMPANY OWNERSHIP

- ☐ A. Does it pass by **Gift to Family Members**? Who pays the tax?
- ☐ B. Should it be **Sold to Involved Family Members**? Do they have the money?
- ☐ C. Should it be **Sold to a Key Employee Group**? Do they have the money?
- ☐ D. Is a **Reciprocal Buyout** with a similar company, practitioner appropriate?

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Stress reduction for running a family-owned business

By Don See

Special to the Business Journal

Working with family members in a business context is twice as stressful as working with complete strangers. In any business, a perceptible amount of tension is generated in daily workplace relationships. Family relationships in the workplace often create special challenges.

All business owners experience the pressures of meeting goals, managing people, and controlling expenses. This produces a natural cauldron of fermenting problems and potential conflict that every manager must learn to handle if the business is to run effectively. Families are groups of imperfect people who occasionally sustain a certain level of interpersonal tension based upon historical factors, i.e., parent-child relationships, sibling rivalry and other assorted conflicts, jealousies and affronts. When family members work together, there is a potential for double trouble that must be overcome through patience and a commitment to the success of the business and to family harmony.

During nearly 30 years of succession planning, I have observed firsthand the most likely circumstance under which submerged tensions will be revealed in a family business – the planned or emergency retirement of the primary shareholder/CEO/parent. Nearly twenty years ago a study of closely-held businesses was conducted by a national business organization to determine the effects of the sudden departure of the head of the company. The study revealed two startling facts:

- Two years after the sudden departure (due to disability or death) of the historical leader, nearly two-thirds of the businesses studied no longer existed.
- The primary reason given for the failure of the companies to survive was “unresolved family conflict.”

How can a family business avoid this outcome? Many families have decided to prepare ahead of time for the eventual retirement of the owner/manager, keeping in mind that due to the untimely death or disability of the owner (or their spouse) the plan may need to be put into effect much sooner than expected, and, on short notice. What are the most important factors that lead to a smooth transition from one generation

to the next?

Share Strategic Information

Every business owner has a wealth of information about key contacts, historical precedent, and special tricks of the trade that have probably never been reduced to writing and may not be known to another living soul. Some of our clients have actually “interviewed” the owner over a quiet lunch and taken notes. Some owners have created a written outline of critical information for the future success of the company. One highly organized client with a new computer prepared a 40-page booklet to share with upper management in the company. The medium is not important, the message is.

Prepare Successor Management

Building into people for their growth and advancement is always a good management style. Strategically preparing top management for the ultimate responsibility of taking over is crucial to the successful transition necessary for an owner to retire. Where owners’ children are working in the company as potential successors, the common wisdom holds true. Give them a chance to work in each of the different areas of the company long enough to learn what goes on and actually do the work. Don’t treat them differently than the other people in the department, neither with more gentleness nor with more harshness. They will get to know the people who may ultimately work for them, and can prove that they are actually capable of helping the company some day.

Establish A Timeline

An owner eventually reaches a decision as to the desired time frame for retirement. It is reached either by analysis of options, intuitive feelings of a deadline, or external factors such as availability of retirement income sources. Once a general deadline is decided upon, the best advice is: Don’t keep it a secret. A timeline can be developed that gives everyone involved a clear sense of the learning curve needed to prepare for

the day when the boss doesn’t show up. It should be flexible, can be general, but should be communicated to potential successor management at the earliest opportunity.

Anoint A Successor

Most owners are reluctant to leave their company until they feel that it will be in good hands. If there are adult children in the company, they may be unwilling to admit that one of them is better qualified or better equipped to run the company. Failure to identify the most likely candidate, however, leads only to confusion and bitterness when the time comes. This extends to the control of ownership in the company also. A good strategic plan identifies the likely successor and provides for the company ownership to be structured in the way that best allows this individual to take over. Sometimes the best successor is likely to be a combination of two or more individuals in specific jobs. That’s fine, but someone has to be CEO; it is difficult to run a company by committee.

When You Leave, Go Away

It’s hard to let go – of anything. It’s particularly hard if what you’re letting go was your baby, your vision, and your reason for existence for the past thirty years or so. Many business owners retire but don’t quit. They come by every day “just to see how things are going.” More likely, they want to make sure that nothing has changed. Many retiring owners wisely arrange for a period after the transfer of the title to remain available for counsel, support, and to facilitate a smooth transition. Beyond that, however, it is good to arrange for an extended cruise, a vacation home in another state, or some device that makes it easy to move on to the retirement phase of life.

Conflict is a normal part of human relationships, and family businesses are not immune. Good planning can create an environment where the conflict is brief, constructive, and leads to a positive outcome.

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