

## The Truth about Small Business Succession Planning

Of all the things facing a man or woman from the moment he or she becomes chief executive officer of a large company, few have a higher priority than determining who will succeed him or her when it becomes necessary.

This is critically important for a large public company with thousands of employees and thousands upon thousands of stockholders. It is no less important for a small company with relatively few employees depend on it for their livelihood.

While large companies typically have board committees and/or staff whose sole responsibility is to develop and implement detailed procedures for identifying potential CEO's both within and outside the company, small companies usually have less structured practices.

They may be as simple as choosing an obvious candidate, such as an only child of the founder or, perhaps at least on an interim basis, the most senior employee if the child is too young. "Though inevitable, succession is often the least planned and, consequently, the most perilous event for a family business," the U.S. Small Business Administration asserts in a paper entitled *Family-Owned Business Success: Leveraging Advantages and Mastering Challenges*. "History has shown that only one in three firms will survive the transition to the second generation. Only 10 percent of the original group will survive into the third generation of ownership."

Given the increasingly complex challenges that small and large businesses alike face these days—whether from government regulation, international competition, new technologies, rapid obsolescence of products, or other factors—simple procedures and searches limited to family or current staff may no longer suffice. In order for a business to have a future, serious issues must be addressed and answered over and over again, often with the help of a financial planner or adviser who can help a business owner through the process. Among these are:

- If a family member is the obvious heir apparent, is he or she really able and willing to handle the job for the indefinite or possible immediate future? "It's never too early to start" training a successor from within the family, the SBA points out. "By elementary school age, youngsters can stuff envelopes and help with office housekeeping chores. As they mature, their participation can grow accordingly...Experts also recommend that the incoming generation work in the broader business world before permanently joining the family venture."
- If the obvious heir apparent is not the best choice, is another family member, perhaps not previously considered, better able and willing to do the job? The decision must be based on the ability of whomever is considered to do the job well, not based on age, relationship, gender, or education. "Separation of family relationships and business is especially essential at this juncture," the agency advises. "The decision must be based on qualifications regardless of family dynamics." Business owners also need a backup plan should family member or other heir apparent fail to run the business appropriately.
- If no family member is able and willing to lead the company for the foreseeable future, does it make sense to look elsewhere within the company before going outside, or does it make more sense to sell the business?
- In former case, would the most senior employee necessarily be the best qualified candidate or would a younger one be a better prospect?
- If no employee is qualified and willing to lead the company at this point in its history and it would become necessary to go outside, would current employees who considered themselves to be eligible become sufficiently disappointed, risking the loss of their experience?

- What sort of compensation and benefits package would it take to attract a suitable candidate, and can the company afford to offer it?
- If the compensation package were to involve equity, does anything need to be done to facilitate consensus among current owners to accept the arrangement? Business owners will need to determine the value of the business as part of any succession planning exercise. Likewise, owners need to structure the sale of the business to children or other successors.
- Given the importance of retaining principal current employees, what plans must be made (a) to properly communicate to them the rationale for going outside and (b) to enhance compensation and/or benefits to keep them? “These key players need reassurance that they have a place after the incumbent retires,” the SBA stresses. “Conversely, incumbents need to help them understand that they must enthusiastically support the succession process and the incoming leadership.”

Recommending that family businesses should begin to plan for succession “a decade or more” before the events, the SBA explains, “Having time to discuss issues and options will increase the odds for success while building family acceptance...”

“Once the succession process is put in motion, the family needs to set a date when the retiring owner cedes full control to the new leadership.”

Retiring founders need to prepare themselves for the changes, too. They will have to move from a time in which their businesses were their lives, where most of their friends were business associates, and where they had few outside interests to a time in which they may find fulfillment elsewhere, perhaps mentoring, or serving non-profit organizations, charitable organizations, or other businesses. Some may want to start all over again, founding new businesses in new fields.

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*This column is produced by the Financial Planning Association, the membership organization for the financial planning community, and is provided by Angel McCall, CFP, a local member of FPA. You will find additional informative articles at [www.AngelMcCallCFP.com](http://www.AngelMcCallCFP.com).*