

# ***SUCCESSION PLANNING***

## ***YOU CAN HAVE IT YOUR WAY***

Like most business owners, you have probably invested a substantial amount of time, energy and financial resources to build up your business. Now that it has become your most valuable asset and source of financial security, have you considered what you personally want from your business?

Is it time to pursue other personal and business objectives? Have you thought about selling your business in order to retire? Perhaps, you want to explore other interests or even start another venture. Do you want to expand your business, raise debt or equity financing, acquire other companies, reduce debt or remove personal guarantees? Alternatively, you may want to "unlock" some of your equity in the business, while still remaining in control.

To protect your family, do you have a plan for business continuity in the event of your death or incapacity? Have you considered a buy-sell agreement coupled with life insurance to fund a buyout of your interest in the business by your management team or a partner?

You can attain these and other personal and business goals through a succession planning process. It begins with an exploration of your needs and objectives. We all have varying needs relating to security, belonging, affection, self respect and self esteem. What are yours? Equally important are your thoughts. For example, what started you thinking about selling your business? Did a buyer approach you? Are you bored or burned out with your business? Does your family business have unsolvable problems?

These basic questions are often challenging and difficult to answer. There are few among us that possess the self awareness to answer these questions alone. Consider the assistance of your spouse as well as a trusted advisor to clarify them.

### *Personal considerations are important.*

Our firm was retained by the owner of a \$10 million in sales manufacturing company who was thinking about selling his company. Started with \$25,000, the company had always been in survival mode. It was profitable, had an 80% market share, consistently grew in excess of 35% per year, and was positioned to double or triple in sales within three years.

Nonetheless, the owner was overweight and concerned about his health. In fact, he was worried about dying. He was also fearful about losing what he had built, as well as achieving further success. Moreover, he wanted to get out of a bad marriage where the primary asset was the business. After a competitor approached him with an unsolicited but low ball offer to buy his company, he started to think about selling. Upon helping him to crystallize his needs, thoughts and objectives, it was clear to him that he wanted to sell. Later that year, we assisted him with the sale of his business.

Once your needs, objectives and other thinking are clear, succession planning options can be developed, evaluated and refined. To plan effectively, you will require the assistance of seasoned professionals knowledgeable in the disciplines of estate planning and business law, taxation and accounting, finance, compensation and benefits, insurance, business planning and valuation.

o develop a course of action that will be responsive to and reflective of your needs, objectives and thinking, there will need to be close coordination among your professional advisors. One of them should take on the role of team quarterback, as well as confidential advisor to you. Then, after a succession plan has been adopted and implemented by you and your team of professionals, you should continue to monitor and fine tune this plan.

There are several alternatives available to you in succession planning to exit from your business. They include:

- Sale of the business to an outsider,
- Sale or transfer of the business to family members,
- Sale of the business to management or partners,
- Sale of all or part (over 30%) of the business to the employees through an Employee Stock Ownership Plan (ESOP),
- Taking the company public through an initial public offering in which you sell a portion of your stock, and
- Continue to grow the business. In addition to building the sales and profits of your business, this may involve raising debt or equity, acquisitions and strategic alliances. This will prepare you to later pursue one of the exit options above.

The goal of succession planning is to ***exit on your terms and on your timetable***. This may involve a time horizon extending out five to ten years.

Start your succession planning process as soon as possible. This will provide you more time and opportunity to put into effect a plan that achieves your goals and objectives, as well as to prepare and position your company for sale or growth. In addition, an early start permits you to fine tune your plan and respond to changing market and business factors. These factors include –

- The business has a positive sales and earnings trend
- A favorable initial public offering market exists,
- A change of leadership is needed,
- The changing business environment necessitates an infusion of capital and the addition of skills for expansion or technology change,
- Competition is eroding your company's market share or profit margins,
- Consolidation in your industry temporarily increases the multiple being paid for companies in that industry
- A downturn in the industry has occurred,
- You have health problems, or
- You cannot solve family succession problems.

### *Some common examples of succession planning.*

he owner loves the business, deriving great satisfaction, joy and self esteem from it. In fact, there is nothing that owner would rather do than remain in the driver's seat. In that case, a succession plan should focus on positioning the company for orderly transition and estate liquidity only after the death or incapacity of the owner. Since continuity of management is essential, transition assumes that a succession management team is in place or can be recruited and retained quickly. Or, it may involve establishing some form of strategic alliance with another company (perhaps servicing a different niche or territory) which, upon the death or incapacity of the owner, will acquire and pay for the business.

For the owner wanting to go public, early preparation and good timing are required. First of all, three years of audited financial statements are required. Then, positive trends in sales and earnings are essential to attract the interests of a good underwriter and obtain a favorable valuation. There is also the need to fill out the management team, preferably including a CFO who has been through an IPO before. You will also want to engage lawyers and other professionals who are experienced in the public markets and who have established relationships with underwriters. Lastly, of course, there must be a robust IPO market. Otherwise, the underwriter will be unable to sell your stock at a fair price or, possibly, at any price.

Then, there is the owner whose business is successful, but wants out later when her business is considerably larger and more valuable. Her succession plan may involve a combination of factors. She needs to groom and niche the company to achieve a higher valuation (i.e., a higher multiple of earnings). She must make acquisitions that not only increase revenues and earnings, but have strategic benefits as well. These may include geographic expansion, market or niche extension, or the acquisition of management, technical or systems expertise. She wants to seek debt or equity financing from sources that will support further growth and acquisitions, or who may become candidates to later acquire the company.

Another common scenario involves an owner who wants to exit. However, the value of her business, savings and other assets are insufficient to fund retirement. Here, the succession plan will focus on building the business to attain a specific target value. Even though this will be a no frills effort, life insurance will be a vital ingredient in this plan to create an estate for the surviving spouse and family of the owner (if that is relevant), as well as to cover the contingency of incapacity. In addition, some form of tax favored retirement plan should be considered.

Business owners can get more out of life and from their businesses. Whether you want to exit your business or expand it, do it on your own terms and timetable. With a team of experienced advisors to guide you through the succession planning process, you can realize your personal and business goals.

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