Succession Planning Process

Each business owner's succession plan will be unique to his/her situation.

Some business owners define their succession planning objective as passing the management and ownership of the business onto the next generation, for others the goal is to sell their business for the best price to a third party. Between these two extremes, business owners have numerous objectives they want to achieve through the succession planning process.

Every business owner should have a plan that details what happens with the management and ownership of the business upon various triggering events. While retirement is often the most cited triggering event, other events including disability, family disruption, premature death and divorce should also be considered when developing your succession plan. Your succession plan may address these triggering events in very different ways. As your personal and business situation changes, your succession plan should be updated to ensure it continues to meet your goals and objectives.

No matter the unique circumstances of each business owner the uniform definition of succession planning is the orderly transition of management and ownership of the business.

Scott Fithian in his book, **Values-Based Estate Planning: A Step-by-Step Approach to Wealth Transfer for Professional Advisors** suggests that the planning process is only three steps: (1) identify goals, (2) develop strategies and (3) implement*.

One of the significant conclusions that Scott Fithian makes in his book is that the most important step is goal setting. The business owner must be clear in respect to what he/she wants to accomplish in various aspects of his/her life. Without clear goals and objectives, advice is without purpose and the situation may evolve in an undesirable direction.

A business owner must plan taking into account the personal side as well as the business side of his/her situation in terms of setting goals and developing appropriate strategies. It is important to align strategies so that personal goals are not sacrificed in the achievement of business goals and visa versa.

The following diagram depicts the three stages of planning while incorporating the two perspectives that must be considered.

It should be noted that there is a looping process between goal setting and strategy development. This looping process is to ensure that the outcomes and side effects of various strategies are reflected upon in terms of goals and objectives. For example, a side effect of a planning strategy that would accomplish one or more of the business owner's goals may be a large charitable gift; however, philanthropy was not a stated goal. This allows an opportunity to reflect on whether or not to update goals or to use this new information or choose another strategy with different side effects.

	Goal Setting Phase	**Strategy Development Phase**	**Strategy Implementation Phase**
	Set goals ▶ / ◀ Reassess goals	Choose an exit strategy ▶	Ownership transition ▶
Personal Steps	• Assess personal & family needs, goals & vision for your business	• Retirement planning • Estate & tax planning	• Family transition planning • Finalize wealth management plan
Business Steps	• Business needs analysis	• Development of options • Establish business value	• Prepare for sale or transition

Continued

What appears to be a simple and straightforward process can be very difficult to start for many business owners. Goal setting and long term planning are not urgent and as such can get set aside. However, some of the triggering events are not at a prescribed time in the future but could befall the business owner without notice.

The best time to plant a tree is 20 years ago; the second best time is now. – Chinese Proverb

Other reasons cited for not starting the planning process are: fear of conflict, fear of change, loss of self-identity, lack of trust in others, lack of vision, conflicting goals among family members, etc. Whatever the reason is for not starting, the benefits far outweigh the time invested.

One method of starting the planning process without feeling fully committed to a big formal plan is to draft a contingency plan. A contingency plan is a reference document that comes into play if the business owner is away for a short period of time.

Consider what would happen if the business owner was travelling in Europe and couldn't get home because of a Volcano in Iceland, or because of a short hospital stay, or because one of the children got sick. The staff at the company would refer to the contingency plan to operate the business on a short-term basis. The contingency plan would outline those items that are critical to the short-term continuation of the business such as: who is in charge, who has signing authority, who should call the key clients, who should inform the bank manager, etc.

A well written contingency plan makes it easier to look further into the future and determine how the business should run without the business owner.

There are generally three components to the succession plan that have to be considered:

1) The management of the company,
2) The control of the company, and
3) The ownership of the company

The management of the company refers to who is making the day to day decisions required in any business operation. Over time a business owner hires more senior people and these people take over the management of the company. Succession is only possible if the business owner has a strong management team in place. This is true if a third party buys the company or the next generation takes over the company; to the extent the business can operate without the business owner stability will be maximized.

The control of the company refers to who is holding the voting shares of the company. This person has the legal power to control the corporation and make decisions about operations, banking, marketing, etc. The person could even cause the sale of the company. Generally a business owner will give up management and ownership early in the succession planning process, but will want control for as long as possible. This is quite reasonable given the value of the business to the business owner's overall net worth.

The ownership of the company refers to who actually owns 100% of the company. Many business owners give up some element of ownership early by "freezing" the value of their interest in the company. A freeze typically leaves the current value of the company with the business owner and the future growth is allowed to be accrued to family members directly or indirectly through a family trust.

If you are a business owner contemplating sale or transition, setting your goals, visions and your exit plan early is critical for success. A succession plan is not synonymous of an estate plan; both should be considered as part of a unified planning discussion.

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For more information, speak with your BMO financial professional.

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* Scott C. Fithian, Values-Based Estate Planning: A Step-by-Step Approach to Wealth Transfer for Professional Advisors. (New York: Wiley, 2000).

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