

Successor Planning Part 5

Last week, I discussed the process of transferring the business in a family. I discussed;

- How to evaluate family members.
- How to establish goals and objectives.
- How to begin the process, and;

The process of setting up a transition plan and making sure that once you begin the plan, you continue it until it's completed.

I also briefly “touched” on the difficulty of a family member taking over in a parent’s “foot steps” – it’s almost like they’re chasing a ghost. In order for that successor to find his/her way and operate the business, they have to make their own decisions, based upon the business needs.

They can not make decisions based upon what the parents would have done, but what he/she believes is necessary for the company to continue to grow and prosper;

- Retiring management should recognize that a successor will have a different leadership style.
- They need to be conscious to “let go”, and;
- They need to have non-family members understand their role.

However, once you commit to let go, you have to let go. You can't jump back into the “thick of things”, if things aren't going the way you want it to; otherwise, the plan will fail.

SELECTING COMPETENT ADVISORS

Let's assume that you finally made the decision to “set the plan” in motion;

- You've identified your goals and objectives.
- You've planned for when you want to exit the business, and;
- You have chosen your successor and are now starting to implement the plan.

Now, it's time to build an effective board of advisors which is paramount to a smooth transition plan. As a business owner, you are going to resist the idea of having the world tell you what to do, because as entrepreneurs, we do not like a lot of input; **however, input is necessary.**

As you're going through the process, it's a normal reaction to want to maintain your independence, your own special uniqueness, and a strong culture of keeping things hidden. I call this the “distrust factor”. How many times have you heard that you trusted somebody (implicitly) and they betrayed that trust?

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in this issue

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However, you need to create a board to assist my transition. You may want to simply set it up as an advisory board who doesn't have the authority to act but only provide advice, and in that situation, you don't have to worry about incurring cost of Director's and Officer's liability insurance.

However, as you start to assemble your team, you need to consider the following questions, which is suggested by the business consulting firm, Re-Generation Partners;

- Are board members independent and objective?
- Do board members have a core understanding of the purpose?
- Will compensation for serving on the board unduly influence any member?
- Are members willing to ask questions, advise and make recommendations?
- Is the CEO in favor of an outside board?
- Is family ownership in favor of an outside board?
- Is the board functioning with a team?
- Are board member's respected peers?
- Are board members qualified to serve based upon leadership and experience?
- Have you eliminated honorary board positions?
- How will you measure board performance?
- Are you going to compensate board members adequately?
- Will board members be able to devote the necessary time to the business?
- Do you have the areas of expertise on your board?
- Does the board have higher affiliate status?
- Does the board have unlimited access to sensitive data?
- Are board members willing to speak out and act as good will ambassador's?
- Is the team adequate to provide continuity?
- Are board meetings scheduled a year in advance?
- Are the financials accurate and delivered on the same schedule each month?

These are certainly a lot of questions to respond to, but are questions that need answers if you want a successful transition.

Ideally, you want your Board of Advisors to play an active, not passive role. They should be able to devote at least 40 hours a year to your business. They need to understand your balance sheet and keep proprietary information confidential and you want them to sign a confidentiality agreement to prevent any problems in the future.

The accounting firm of Grant Thornton published an article entitled "Changing Roles for Board of Directors and Entrepreneurial companies" which sets out the "rules of the road" to use in soliciting the best help from advisors, particularly if your company requires a more formal relationship. I believe Grant Thornton published that report in 2002 or 2003 and I'm sure if you are interested in utilizing their services, they would be more than happy to provide you a copy of that article.

THE ASSET TRANSFER

By 2010, American businesses are likely to under go the largest generational transfer of wealth in its history – between \$6 trillion and \$12 trillion, according to various economic reports. A large portion of these financial windfalls is invested in family and closely held businesses that were founded by a generation of entrepreneurs after World War 2. **In fact, 1946 was the year most often cited in the survey by Arthur Anderson in which they stated 1951 was the medium year for business formation.**

There are 3 basic choices in business succession;

1. Keep the business in the family.
2. Create internal management to perpetuate the business and possibly sell the company under an ESOP program;
3. Sell the business to an outside interest.

Different succession plan strategies offer different tax and financial benefits to a business owner.

Strategically planned stock gifts, for example, can protect owners from probate and related assets.

Buy/sell agreements can provide the estate and business liquidity while recapitalization can insure that the resigning share holder will collect the dividends in the future. Other succession plans include;

- Stock prevention.
- Reorganization.
- Stock sales.
- Charitable transfers.
- Private annuities.
- Employee stock ownership plans (ESOP's).
- Trust.

As you start the transition process, you may initially become overwhelmed. However, you need to recognize that;

- You need a set of advisors to walk you through “the process”.
- You need competent legal and accounting assistance, and;
- **Whether you utilize Ahern or someone such as Ahern, you need someone that can guide the family through the challenges you are going to experience throughout this process.**

It's important to recognize that one size does not fit all!

ESTATE PLANNING

As part of any successor plan, you have to ensure that your estate is in order. The essence of estate planning is to make it easier for your accumulated wealth and assets, to pass to future generations. **Minimizing the tax burden will maximize your assets,** but unfortunately, it's often a subject that is too often overlooked by many closely held businesses.

In fact, approximately 23% of senior-generating share holders of closely held businesses have not done any estate planning other than writing a will. Nearly a quarter of that senior generation have only some understanding of the amount of estate taxes due upon their death.

In addition, nearly quarters of those people do not know each other's estate plans and transfer intentions.

A survey by a "payment" company identified that the most common estate planning mistakes made by business owners consist of;

- 38% have no succession or transition plan.
- 24% fail to plan.
- 16% have failed to minimize taxes or lack the knowledge of tax laws, and;
- 14% have insufficient cash flow to transfer the business.

One of the things you need to consider when planning your succession is to minimize the "tax bite". This is an extremely difficult process because you're discussing about planning your taxes after you've passed on; **nobody likes to talk about that, it's a very uncomfortable feeling.**

As I've stated previously, selling your business is like planning your own funeral. It's a very difficult process, very emotional and unfortunately, when you get to this stage of your life, a portion of your life has passed; none of us like to admit we're getting old.

Assuming that you've made a conscious decision and still want to go forward, you then need to address what will happen to your business when you die. It's important to understand that the Internal Revenue Service will value your company at your death and we all know that the government is strapped for cash. **The full value of your interest in your company will be included in your taxable estate.** For a successful business that IRS value may run into the millions of dollars. That's why it's important to have somebody that is competent in the transportation industry to value your business as part of the successor planning process;

- The IRS does not have access to the records of the private sector.
- They look at the "public" sector.
- **They value a business based upon if you are performing like a public company, and;**
- Therefore, they base their value on what may be inflated values.

Unfortunately, private companies do not sell for what public companies sell for. Also, it's important to have the review updated every few years. For example; a trucking company that was valued in 2006, certainly does not have the same value in 2009. **The reason is obvious – the economy is in the toilet.**

As you're choosing someone to do this very important "process", we have a tendency to engage our Accountant. Accountants are a very fundamental part of this process. However;

- If your accountant or accounting firm does not have extensive experience in transportation;
- They have not been involved with numerous sales, then;
- Do not utilize their services for the evaluation – utilize the service of someone that has specific expertise in transportation.

The same applies when you're utilizing a law firm;

- Utilize a law firm that specializes in transportation or has a special division that's involved in transportation and logistics.
- Don't use a general practitioner, and;
- Don't necessarily use someone that you're neighbor recommended.

Use somebody that understands the components of our industry.

I can't impress upon you how important this is, particularly since trucking is going through a major recession and values have significantly changed. Engaging a specialist to assist you in this process, that understands the trucking industry, is critical to completing this process.

In closing, next week I will touch on the components of capital gains and estate taxes, etc.

QUOTE OF THE WEEK: **“A job becomes work only when you worry about it.”**