

Business Succession Planning

Question: My wife and I own a small business. We are at that stage where we want to retire and enjoy the fruits of our labor. What are some ideas that we can explore to start the transition to the next phase of our life?

Answer: If you are a small-business owner, you have probably poured much of your life into building a successful enterprise. You may be reaching a point where you have thought about retiring. Like most business owners, you are probably counting on your company to be a significant resource that helps to fund your retirement.

Business owners face unique challenges that complicate retirement. While employees in a company can simply leave and take their workplace retirement savings plan with them, the situation is far different for a business owner. In effect, your retirement may very well be tied up in the day-to-day functions of the company. A small business needs a succession plan in place so that owners can get the true value out of the business when the time comes.

Creating a succession plan for a business can vary, depending on the company makeup. If you are a sole business owner, the issues you face will differ somewhat from a business where multiple owners are involved. If you're involved in a family business, there are separate considerations that are unique to the business process.

One point is paramount when it comes to business succession: Planning ahead is necessary. Owners need to carefully think through not only how they would like to pass on their business some day, but any number of contingencies that might come into play. While there is no requirement that a business survive the participation of the owner, it is a much more valuable asset in terms of funding retirement if the business continues. Begin by considering who will take charge of the business. You have any number of options to consider:

- Selling your business to another firm, perhaps a competitor
- Liquidating your interests by having another partner buy you out
- Having a family member take over the business
- Turning the business over to other company employees

In each of these scenarios, the big question is, "How will I get my money out of the company?" The time, energy and resources you invested in building the firm should pay you back when you retire. But this can only happen if you plan accordingly. Too many times, business owners approach retirement with no succession strategy in place. Then they find it difficult to obtain the type of payoff deserved from years of hard work building the business.

While the idea of selling off a company to another firm sounds like the easiest way to cash out, it is not a realistic option for most businesses. Those types of transitions rarely occur, and it is not something you can plan on. A more likely option is to determine how others who succeed you in running the business, whether family members or other employees, could buy out your interest in the firm. You need to consider drawing up an agreement between yourself and other business partners or possible successors. Open and honest discussions between involved parties are important, and the help of a qualified legal professional will be required to draw up necessary paperwork.

Another business succession strategy that should be developed is a method of business continuation in the event an owner dies. Just as a death can catch a family off guard, the same is true with a company. Life insurance can be a vital component in helping to keep a business on track if a sudden death of an owner occurs.

One of the trickiest situations can involve the death of a business owner that leaves other business partners behind. Steps should be taken in your firm regarding the ownership position when one owner dies. In this situation, you should explore the benefits of having life insurance policies purchased on each of the owner's lives. The proceeds of such a policy will provide surviving business owners the cash needed to buy out the deceased owner's share of the company. One benefit is that surviving partners will not suddenly have a new partner, an heir to the deceased business owner. That can create an awkward situation for the business. A life insurance solution may also be needed to protect a business owner's family if no other partners are involved in running the business.

Any business succession plan involves one vital piece of information: the current valuation of the company. It is important to have a proper valuation placed on the firm before structuring any sort of business succession agreements or purchasing life insurance policies. This is a process that requires straightforward accounting to determine the real worth of the business. A financial adviser may help you develop a plan for your business, including a succession plan.

Posted in The Times-Picayune June 18, 2008. John Gin is a certified financial planner based in New Orleans.