

## Transition Issues in a Family Owned Business

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My son-in-law wants to join me in my business. I could use some help with the business. I'm just not sure if this is right for either of us. What should I do?

We talked with the owner and got some additional details. The business is over 20 years old, stable and successful. Each year the company has grown a little more reaching \$1 million in revenue nearly 10 years ago. The company provides a good living for the owner, who is careful about managing the finances.

The owner, who is in her early 60's, sees some industry changes that concern her. And she is starting to think about when, and how, she will exit, in about 5 years. It appears that the owner will need more income from the company in order to retire comfortably – whether from increased bonuses over the next several years, or from a sale. The son-in-law currently works for another small business.

Let's start with some facts about family owned business. Then we'll look at turning over business ownership, from one generation to the next. We'll wrap up with some things this owner can do, to increase her chances for success, should she decide to bring in a relative.

Between 70% and 90% of all businesses in the United States, today, are family owned. They range in size from 2 employees to

major corporations. Most of the businesses in Westchester and Fairfield County are family owned. They are a backbone to our local economy.

Unfortunately family owned businesses are tested by transitions. Less than one in three survives the transition from founder to second generation, and we lose another ½ in the transition from second to third generation. Out of 6 family-owned businesses, only 1 makes it from founder to successful operation by the third generation of owners.

Several factors impact a successful transition: viability of the business, planning, desire on the part of the founder, desire on the part of the next generation.

Is the business viable? While many owners operate successful, thriving businesses, others run marginal businesses, with little likelihood for expansion. Some businesses have outlived their high points, while others have bright futures ahead. In some cases, the problems the business faces are fixable. In some, they are not. It is important to know the difference.

Is there a plan for the transition? Buyouts take time, typically years, and a well thought out plan, to effect a successful transition.

Goals of a successful buyout include managing cash flow. It is

in everyone's interest to preserve the funds the company needs to grow, while helping the exiting owner to build a nest egg outside the business.

Another buyout goal is to transfer knowledge and authority. The next generation has to demonstrate financial, managerial and leadership skills. They need time to learn about the company's products or services, and about selling and managing customers. Professional education and on-the-job training can prepare the next generation for take over, if properly planned out.

Then it comes down to intention. Is the senior generation ready to let go? Is the next generation ready to step up? Often, I find, the mind says yes, but the heart hasn't caught up. Retiring is emotional, and often includes questions about mortality, self-worth, importance, and usefulness. Stepping into the big footprints of the previous generation can be intimidating. And in many cases, stepping up may not be what the next generation had in mind for their future.

In this case, there is one more loaded issue. The incumbent is not a blood relative. He is a son-in-law. While he is in a good marriage, the odds of that succeeding are only 50% in today's world.

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So, what can our reader do to insure success? Start with a realistic assessment of the business. Is it viable? From what I know, I believe it is, although changes will have to be made to grow it and take better advantage of the client base.

Next, the owner needs to have a series of conversations with her son-in-law about his intentions. Where does he see himself in 5-10 years; what are his personal goals? Is he committed to this business, and doing what it will take to succeed? They also need to discuss what would happen, in the case that the marriage does not work out. Should the marriage fail, will there be problems financially? How will the current owner feel, having a non-family member running her company?

Finally both parties need to assess the son-in-law's level of preparedness – not just for running the business as it is today, but for running a business 2-3 times the size. Ask the son-in-law to assess the challenges and opportunities he sees in the industry, and the company, and to share his thoughts on how he would deal with that. They need to decide what he would have to learn, and assess his ability, desire and commitment to learning.

If they both agree it makes sense to go forward, they need to build a timeline and training plan that

takes advantage of the owner's willingness to be involved for another 5 years. The current owner will want to develop a picture of what life will be like, when she no longer comes to work, so that she has something to work towards. Together they can build a transition plan that phases her work commitment down to part time, and increases the level of actions and decisions for her son-in-law. They need to set out realistic goals and milestones for the business, which challenge the son-in-law, and provide regular assessment as to how he is doing. They want to agree now, to rules about how they will handle any future disagreements. And, they need to build a financial plan, including advice on tax and estate planning, that insures a healthy future for both parties, with rules about transitioning ownership and payout.

Looking for a good book? Try *Family Business Succession: The Final Test of Greatness*, by Craig Aronoff, Stephen McClure, and John Ward.

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