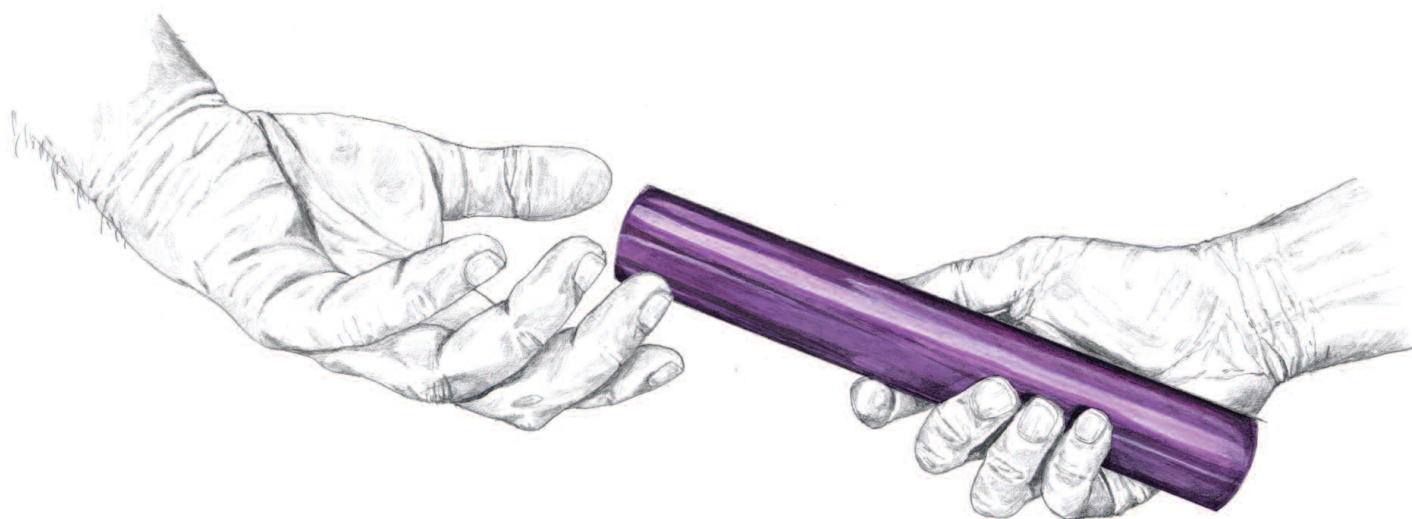


# Succeeding at succession

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A Grant Thornton series for privately held businesses January 2010



“Running a private business in today’s market is very different than it was 50 years ago, or even 10 years ago. Against the backdrop of the credit crunch, recession, globalisation and the internet, businesses are under more pressure than ever. Competition is global, fierce and well-funded. If you do not address these issues as part of your succession planning process, your business may pay an irretrievable price.”

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**David Brooks**

Grant Thornton, United Kingdom

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Data in this paper utilises findings from the Grant Thornton International Business Report. This is an annual survey of the views of senior executives in privately held businesses (PHBs) all over the world. Launched in 1992 in nine European countries the report now surveys over 7,200 PHBs in 36 economies providing insights on the economic and commercial issues. To find out more about IBR and to obtain copies of reports and summaries visit: [www.internationalbusinessreport.com](http://www.internationalbusinessreport.com)

# Knowledge that stands the test of time



For several decades, Grant Thornton firms worldwide have focused on fuelling the growth of privately held businesses – a broad market segment that includes family enterprises, investor- and entrepreneur-owned businesses and professional firms.

Inevitably, privately held businesses owners seek an effective transfer of ownership at critical stages of the business cycle or as their personal ambitions develop. Without an effective plan, the future of the business may be put in jeopardy or the owner may suffer adverse financial or tax consequences.

Conversely, effective succession planning will provide the business with a greater likelihood of survival and ensure a better financial return for the owner.

This paper will highlight for you the factors that need to be considered to ensure the future success and legacy of privately held companies. Much of this information is supported by the findings of the annual Grant Thornton International Business Report (IBR), which provides insight into the thoughts and opinions of 7,200 business leaders from 36 economies.

Grant Thornton are experts in the preparation of succession plans and helping to address many of the issues arising – such as helping to value and sell the business; assessing the right structure going forward; and dealing with the psychological factors that arise if the business is passed on to family members. Talk to us if you are considering the future plans for your business.

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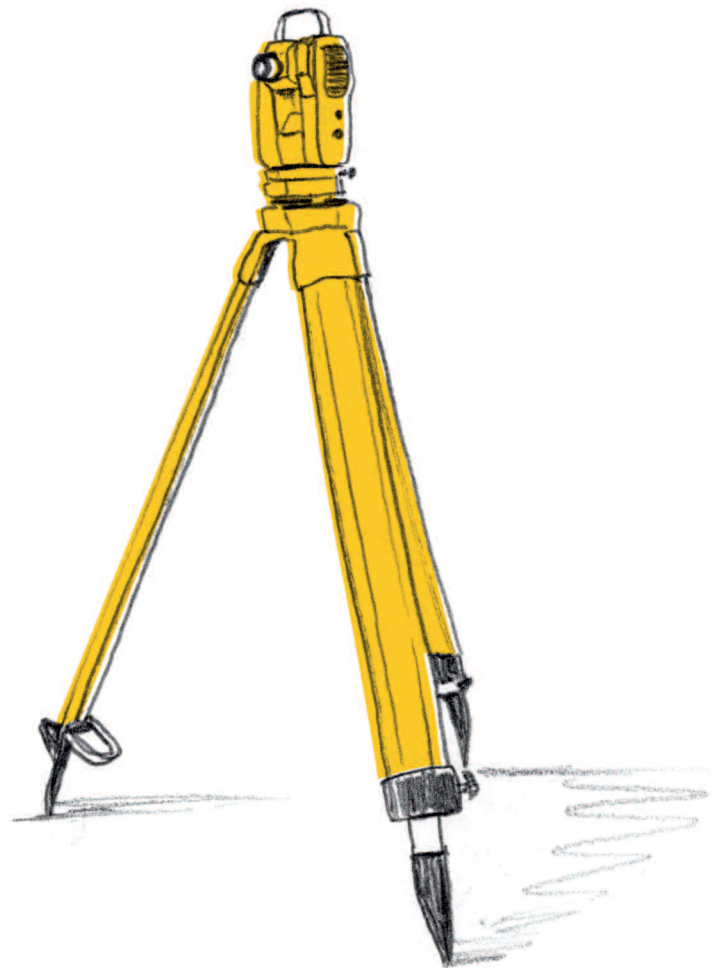
**Alex MacBeath**

Global Leader, Grant Thornton International, markets

# It took time to build the business. It takes time to pass it on

What do UK music company EMI, US confectionary giant Mars Incorporated, Canada's Irving Oil and Greyhound Australia have in common? They are all highly successful private companies that have stood the test of time. EMI was founded in 1887 by Emile Berliner, who previously developed the microphone for Alexander Graham Bell's telephone. Mars got its start in 1911 in the Tacoma, Washington kitchen of Frank Mars. Irving Oil was established in 1924 by K.C. Irving and remains a family-owned and privately-held company. And with over 100 years' experience, Greyhound Australia is one of the oldest coach companies in the world.

These companies are in different countries, in different sectors and have different operating models, but they share one thing in common: a commitment to building a business that lasts beyond the tenure of its founders. Creating this type of legacy does not happen by accident. It requires a careful nurturing of your business value drivers, a clear articulation of your personal and business goals, the identification and grooming of qualified successors and the support of specialised advisers. This is what succession planning is all about.



# Answering the difficult questions

Although succession planning can be simply defined as the process of transferring the control and ownership of a business, developing and executing a succession plan is not nearly so simple. As the owner of or investor in a privately held business, you need to answer some hard questions. For instance, how long do you want to stay in the business? How sustainable is the business model going forward? Have you identified managers capable of growing the business into the future? How will these decisions affect key employees? If you run a family business, you also need to consider emotionally challenging issues that may call the skills of your family members into question or require you to creatively structure your succession to be fair to all your children, understanding that fair and equal are not the same thing.

These issues may be complex, and sometimes uncomfortable to consider, but ignoring them won't make them go away. And while solutions exist to these quandaries, they won't appear overnight. If you want to ensure the long-term survival of the business, minimise taxes and – for family enterprises – maintain healthy family relationships, it's never too early to put a succession plan in place.

To help you tackle this process, step-by-step, Grant Thornton has developed this first paper in what will be a series on succession planning topics. In this paper, we present an overview of succession planning and explain how Grant Thornton firms can help you create a platform for building a sustainable, long-term business while maintaining both financial and emotional stability.

Most popular type of change in ownership – global average percentage

	Trade sale	Bring in private equity/bank investors	Flotation/IPO	Sell/pass to family member	Management buy-out/buy-in	Sale to employees	Merger	Other
<b>2009</b>	18	14	8	23	13	7	9	6
<b>2007</b>	25	20	15	15	16	10	16	7
<b>2005</b>	24	19	9	18	12	8	20	11
<b>2003</b>	14	13	7	16	7	7	21	12

Base = all anticipating a change of ownership  
Source: Grant Thornton International Business Report 2009

Sale to, or passing the business to, a family member is now the most likely method of changing ownership for Privately held businesses (23 per cent). This method was the only one to have increased in popularity since 2007.

All other methods of change fell in popularity. Trade sale, the most popular method in 2007, dropped seven per cent from 25 per cent to 18 per cent in 2009. Mergers and flotations/IPOs were similarly unattractive compared to 2005, both falling by seven per cent to nine and eight per cent respectively suggesting that the economic crisis has changed the strategies of many PHBs as their businesses fall in value.

# What's stopping you from getting started?

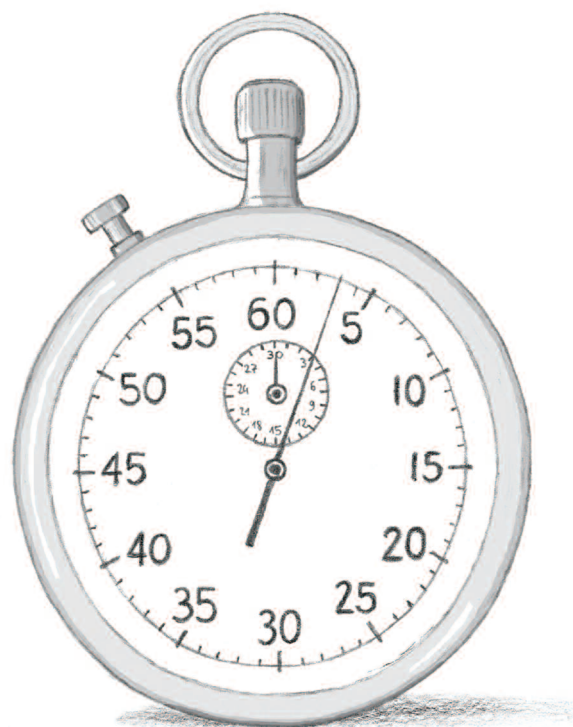
The numbers tell a startling tale. According to the Grant Thornton 2009 International Business Report (IBR), 25 per cent of private businesses expect a change of ownership within the next ten years. Yet only just over a half of these companies have a formal succession plan in place. These numbers are supported by other independent research studies in countries as diverse as New Zealand, the United States and Canada. This may explain why only 30 per cent of private enterprises survive into the second generation and only 12 per cent survive into the third.

The truly interesting part of this story lies in the reasons business owners cite for failing to develop a succession plan. They worry what will happen in their absence, who will be responsible and how the business will fare after their departure. They are concerned about meeting the needs of both managers and family members who are not in line for succession. They are uncomfortable about discussing personal and financial goals or about disclosing family issues to outsiders. They are afraid of compromising their personal relationships or creating irreconcilable rifts. Very often, they are simply hesitant to retire, concerned about their financial prospects or feel that any identified successors are not ready to take control.

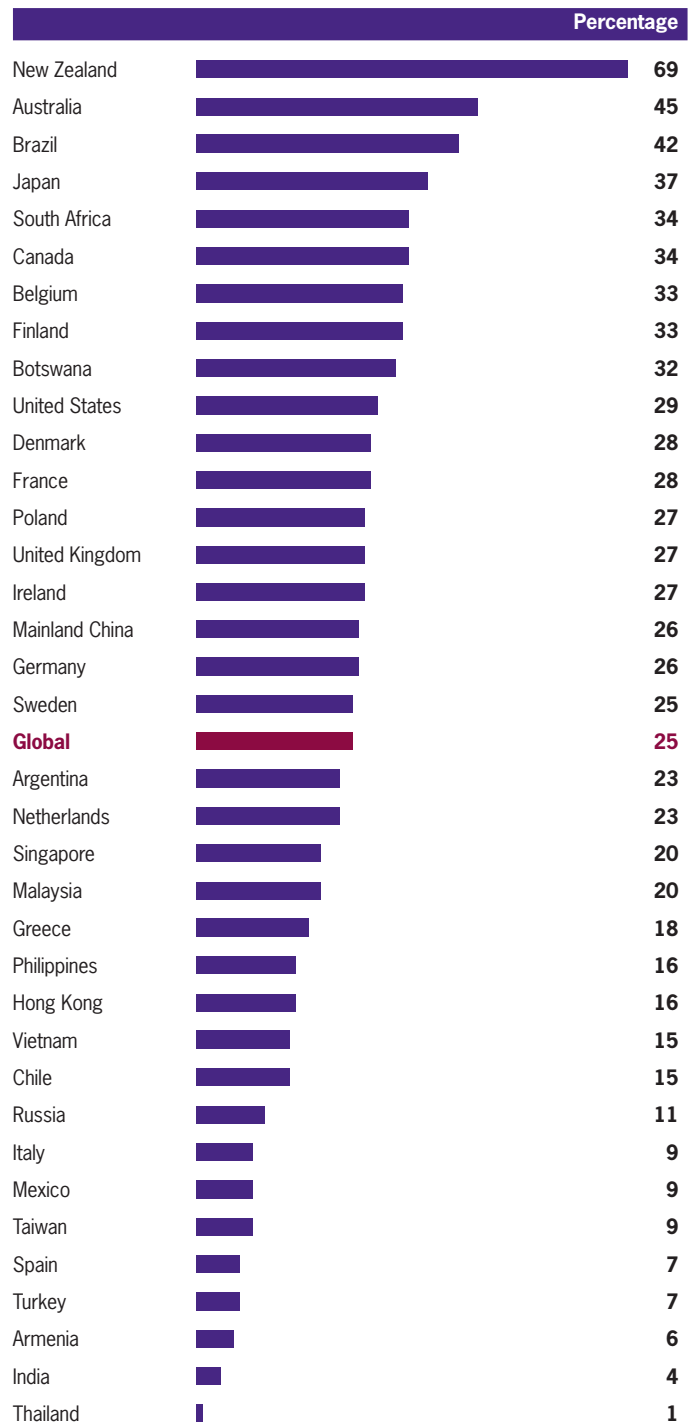
“If you want your successors to be ‘ready’ to take control, you need to give them the opportunity to work in the business. You need to give them sufficient free rein to make decisions – and, more importantly, make mistakes. You also need to provide them with a governance structure that defines their roles and responsibilities in clear and measurable terms.”

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**Bobby Stover**  
Grant Thornton, United States



Percentage of businesses expecting a change in ownership in the next 10 years



Source: Grant Thornton International Business Report 2009

While these challenges are not as acute for investors in privately held businesses, owners of non-family businesses or managers of professional services firms, even these companies must grapple with the complexities of identifying appropriate successors, defining clear exit strategies and laying the foundation for future growth. Often, the day-to-day realities of running a business hamper efforts at this type of long-term planning. As a result, many privately held businesses find themselves making succession-related decisions under pressure, rather than planning in advance.

Additionally, many businesses now point to recent economic volatility as a reason to defer succession planning. Arranging to sell or merge a business amid historically low valuations can be daunting. In a worst case scenario, without a sustainable strategy for the future and a viable business model, planning for succession becomes a moot point.

The Grant Thornton International Business Report found that one quarter of PHBs expect a change of ownership in the next ten years. While there is no significant regional pattern, differences between countries are marked, ranging from 69 per cent in New Zealand to one per cent in Thailand. Second to New Zealand, but well behind at 45 per cent, is Australia with South Africa also appreciably above the global average at 34 per cent.

In the European Union, the Mediterranean countries featured among the lowest expecting a change of ownership (Spain at seven per cent, Italy nine per cent and Greece 18 per cent). Northern European countries tended to be above average but only Belgium and Finland at 33 per cent were markedly so.

Latin America showed great diversity with Brazil (42 per cent) in third place and Mexico (nine per cent) and Chile (15 per cent) in the bottom ten. In Mexico, the outcome was surprising since in our 2005 survey the country was in joint third place with 47 per cent.

Although many of these reasons appear valid, failure to act can result in a host of unintended consequences. Without taking time to maximise the value of the company or adopt a structure that supports future growth, you may find yourself unable to attract buyers or investors. This may also compromise the company's ability to continue compensating owners following their exit – putting their financial welfare at risk. Without developing an appropriate leadership structure or properly preparing successors, the business may flounder and ultimately fail – compromising investors' ability to realise a sufficient return on their investment. Without gaining buy-in from all the key stakeholders, you risk losing essential staff or alienating family members in a family-owned business. And without planning for contingencies and considering all your alternatives, you can face a forced sale, higher tax payments and the potential dissolution of the business you worked so hard to build.

“Business owners and investors are used to making firm decisions and boldly heading along their chosen path. However, when it comes to succession planning, this can result in unnecessarily locking yourself into a course of action without considering the full range of options. Independent advisers can help stakeholders widen their view by presenting different approaches and solutions.”

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**Tony Markwell**  
Grant Thornton, Australia

For these reasons and more, succession planning is not a process that can be put off. By laying the groundwork in advance, you can position the business to capitalise on opportunities as they emerge, regardless of economic conditions. For instance, with a succession plan in hand, some privately held businesses were able to take advantage of recent market volatility to minimise the duties and taxes that would otherwise have arisen upon the transfer of their companies.

At the same time, it's critical not to underestimate the challenges that can arise as you begin to plan for succession. To improve your odds of success, you need to approach succession planning as an ongoing process, taking steps to overcome the psychological barriers and consider your options from all angles.

# Following a structured approach

To get a handle on the complexities associated with succession planning, it helps to start by taking one step at a time. Although different approaches to succession planning exist, private businesses are more likely to reach their goals by following a proven process. The following process, recommended by Grant Thornton firms, is designed to help you uncover your real goals and objectives:

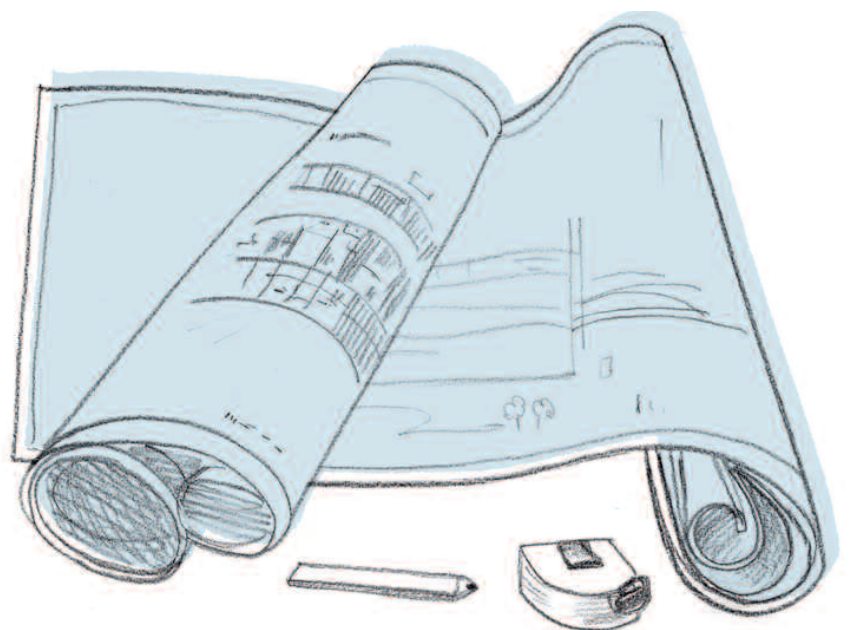
## 1. Collect and analyse information

In this first phase, you (or your advisers) would conduct a series of confidential interviews with business owners, key management and/or family members to uncover both your immediate and long-term objectives. From an operational perspective, this allows you to identify potential obstacles to your intended succession plan and put processes in place to resolve them. From a personal perspective, it ensures that current wills, shareholder agreements and financial resources reflect your aims. This phase also affords you the opportunity to “meander through your mind” to uncover the factors that truly underpin your business philosophy, family relationships and personal concerns.

“Transitioning a business is no small item to plan around. If you don’t do this right, it can scuttle the successful transfer of the business from one generation to the next.”

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**Bill Kingsley**  
Grant Thornton, United States



## **2. Assess strategic and wealth enhancement opportunities**

The second phase involves brainstorming a range of potential solutions with your advisers which will address your succession planning goals. Through strategic planning sessions with your key personnel and/or the creation of a family council, you can solicit input from all your stakeholders to ensure your plans take everyone's varying needs into account. This second phase also helps you consider opportunities to improve the value of the business over the short, medium and long terms by identifying the actions you can take to improve cash flow and reduce perceived or actual business risk.

## **3. Design, develop and implement your plan**

Once you have considered the various options, you should have the information you need to begin plotting your succession strategy or building a “blueprint” of the plan you are going to implement. At this stage, the steps you take will depend on the structure you've selected for your succession. For instance, for family-owned businesses, if you plan to pass the business on to a family member, this is the time to identify your successor and help them develop the expertise they need to assume control of the business. For owners or investors who plan to sell the business, this is the time to put processes in place to maximise business value – from benchmarking against your peers, rationalising business lines and identifying service gaps to shoring up your balance sheets, extracting personal assets from the business, generating competing bids and, if selling internally to management or other family members, arranging for the financing required to effect a successful transfer.

If you've given yourself a long enough runway, you also can enhance the odds of reaching your succession planning goals by developing parallel succession plans – one that can be implemented immediately in the event of an unforeseen emergency; a second that you can implement in the mid-term (within one year) to begin closing any identified gaps; and a third that lays out your long-term intentions (five to 10 years) and contemplates a variety of financial models that account for different contingencies or scenarios. Here is where a proven process is invaluable. Many strategic plans, business models and succession plans never make it from concept to reality.

#### 4. Review and monitor

Once your plan is in place, there is still more for you to do. As the business and/or family dynamics change over time, your succession plan must change with them. Be sure to schedule regular reviews of your plan to ensure it remains current and continues to reflect your evolving wishes. Be sure, too, to communicate any change of plans to your key stakeholders so no one is blindsided when the time for a business transition arrives.



Percentage of PHBs with a formal strategy in place ready for change in ownership

	Percentage
European Union	55
NAFTA	60
Latin America	40
Asia Pacific	45
Nordic	42
Global	52

Base = all anticipating a change of ownership  
Source: Grant Thornton International Business Report 2009

Among businesses expecting a change in ownership, just over half have a formal strategy in place. North American Free Trade Agreement (NAFTA) countries are most prepared with 60 per cent of PHBs having a strategy in place. Least prepared are PHBs in Latin America, where just 40 per cent of PHBs who expect a change actually have a formal strategy in place.

# Taking action is the most important first step

Although there is no definitive “how to” manual for developing an effective succession plan, our experience shows that the following actions can help the business survive – and thrive – into the future.

## **Start early**

Succession planning cannot be approached as a one-time event. Instead, it is a process that should begin long before the owners plan to exit the business. Starting early also ensures you can select from the widest range of options available to you.

## **Commit your time**

Getting the business to its current level took time and commitment. A succession plan needs the same attention.

## **Identify your business value drivers**

By understanding which parts of the business will be most valuable to a purchaser or other potential successor, you can maximise the value of those assets in advance.

## **Articulate your core values**

One way to ensure the business maintains its focus and follows the path you envision is by clearly articulating your core values and instilling them among all your staff.

“Succession planning can be overly complex if it is not approached in a rational and organised fashion. Owners, investors and managers must take the time required to both develop a succession plan and implement it by putting processes in place to effect a successful transition.”

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**Alejandro Chiappe**  
Grant Thornton, Argentina

## **Rely on decision-making frameworks**

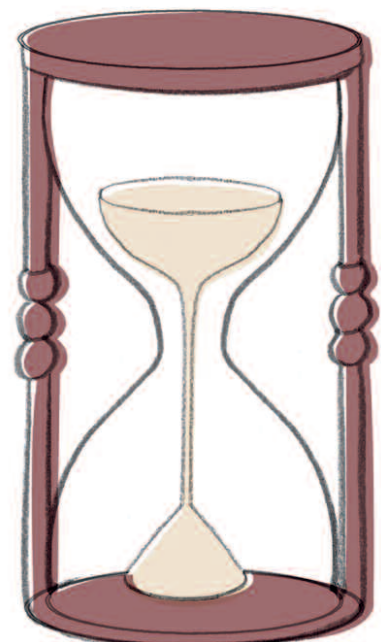
These can help strip the emotion out of your decisions and provide a roadmap for your successors to follow.

## **Involve your successors in your planning**

When key employees, family members and potential investors understand your intentions, they are more likely to support your decisions.

## **Separate your business and family assets**

This involves more than adopting internal control processes and performance management practices. It may also mean introducing more formal operating processes – from the establishment of shareholder agreements and employment agreements to holding regular board meetings.



# A step-by-step guide

As part of adopting a structured approach, your advisers work with you to address each step of the succession planning process. These steps are discussed in greater detail in the remaining reports in our succession planning series, and include:

## **Establishing the value of your company**

Before you even begin planning for succession, it's imperative to ensure that the business is sustainable into the future. This goes beyond cleaning up your balance sheet or strengthening your internal controls. In today's volatile economic climate, businesses must have a clearly articulated plan for long-term growth. This is particularly true for privately held businesses contemplating the viability of creating an organisation capable of surviving over time. These issues all play a role in helping to determine the value of the company.

## **Establishing your goals and objectives**

When setting goals, it's important to consider not only your staff's (and/or family's) needs, but also your personal objectives for wealth preservation and optimisation. Working with unbiased external advisers can be especially important at this juncture given the highly emotional challenges that often arise, particularly among first generation owners.

## **Identifying and incentivising potential successors**

Whether you are considering family members for succession, promoting internal staff members or seeking external management, you must develop a plan that works in your business's best interests while keeping emotions in check. This encompasses not only identifying successors with appropriate skill sets, but also communicating these roles and responsibilities to all stakeholders and providing your selected successors with sufficient training to support continued business growth. Designing a compensation package to reward performance is also appropriate at this stage.

## **Selecting an appropriate structure for the succession**

The structure you select for your business transfer will depend on the objectives you are trying to achieve. For instance, if you transfer control while retaining ownership, you may provide management, investors and other stakeholders with confidence that the organisation's vision will remain on track. Conversely, a transfer of assets can help you potentially minimise your tax burden.

## **Scenario planning**

In business, as in life, things rarely go exactly according to plan. That's why your succession plan must be flexible enough to change when circumstances shift. This involves preparing for a wide range of contingencies – from a loss of leadership or unanticipated illness to ensuring you retain continuous access to the cash flow you need following your transition.

## **Minimising taxes**

Depending on your country of residence, the tax implications that can arise on the transfer of shares can be significant. By structuring your transition in a tax effective manner at the outset, you can minimise both corporate and personal taxes. Family-owned business also can use this stage to provide for the family's needs after they exit the business.

# Don't leave things to chance

Although planning for succession can be complex and daunting, working with the right advisers can make all the difference. With our global reach, proven track record, integrated suite of services and in-depth knowledge of privately held businesses, Grant Thornton member firms are uniquely positioned to help you reach your goals. Beyond offering you solutions that range from estate and tax planning to business advisory and wealth management, as well as looking after all aspects of the sale of your business, our practitioners truly act as your trusted guides to help you navigate the succession planning process. By developing personal relationships, we gain an intimate understanding of the psychological

factors and emotional hurdles that come into play during this challenging time and can help you resolve them in a way that accommodates all your stakeholders' needs. Our extensive succession planning experience also means we have the know-how to propose a huge range of options that can deliver creative solutions to the most intractable problems.

When it comes to something as important as succession planning, you can't afford to leave things to chance. Find your local Grant Thornton specialist through the global reach section of [www.gti.org](http://www.gti.org) or contact: [amacbeath@grantthornton.ca](mailto:amacbeath@grantthornton.ca) to find out how we can help you succeed at succession.

## About Grant Thornton

Grant Thornton International is one of the world's leading organisations of independently owned and managed accounting and consulting firms. These firms provide assurance, tax and specialist business advice to privately held businesses and public interest entities. More than 2,600 partners provide clients with distinctive, high quality and personalised service in over 100 countries. For more information visit [www.gti.org](http://www.gti.org).

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“Many private business owners are loath to spend money on a succession plan they feel they won’t need for many years. However, by exploring the various options available, a succession plan often provides owners with a preferred blueprint. It consequently needs to be viewed as an investment capable of delivering significant benefits – such as increasing the value of the business, being nimble enough to contemplate a sale if the opportunity arises and gaining the ability to deal with any other shareholders or family members in a more proactive and responsible way.”

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**Kay Gray**

Grant Thornton, Canada



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