BUSINESS SUCCESSION PLAN MODEL

I. WHAT IS A BUSINESS SUCCESSION PLAN

A Business Succession Plan is a multidisciplinary process providing a comprehensive and strategic approach to guiding the transition of business ownership. It is to be a dynamic document that is utilized as a guide to manage the issues of transition. When a succession plan is in place, it allows the business owner to anticipate and effectively manage change.

A successful plan must be realistic and workable and not prepared in isolation. It must involve family members, professional advisors, shareholders, partners, strategic employees, and all stakeholders in the business.

Communication, during the preparation and upon completion, is a critical component of the process. Unless all affected parties are clear about what is in the Succession Plan and have had the opportunity to participate in its preparation there will be problems.

The Plan will address the issues of "When and How" transition of the business to new ownership and management will occur.

II. HOW TO USE THE BUSINESS SUCCESSION PLAN MODEL

The Business Succession Plan is to be used as a model or guide to lead the user through the process of developing a Succession Plan for their business. As each business and owner is unique, the Plan will also be unique. The model is a tool that will be customized to the personal needs of the user.

Use of the Model will assist the business owner in the preparation and gathering of information necessary to make informed decisions regarding the future of the business. It should not be viewed as being a replacement for using professional advisors. The implications regarding legal, financial and taxation issues are too great and intricate to be made without professional input.

III. WHY PREPARE A BUSINESS SUCCESSION PLAN?

A Business Succession Plan is an important component of any business' strategic planning process. It will aid the business owner in preparing for the time when they will retire from the business or in more extreme times, of illness or death. With a Succession Plan in place, the business will be more likely to survive through transition of ownership and will maximize the return to the retiring owner's investment.

By not preparing a Succession Plan, business owners risk monetary loss through ineffective tax and financial planning at the time of succession. In many instances the future of the business may also be put in jeopardy.

Transition to new ownership, whether within the family or to outsiders, is always a risky proposition, however, through effective planning the risks can be reduced and contingencies put in place.

IV. COMPONENTS OF THE BUSINESS SUCCESSION PLAN

Each Business Succession Plan will be unique as each business and personal situation is unique. The components of the Plan, which are outlined below, provide a guideline to be followed, however, not every section will be required by every business and may be modified to meet personal needs.

A. ESTABLISH GOALS AND OBJECTIVES

This section of the plan is where the owner's personal goals and vision for the business and his/her future role in its operation will be addressed. The establishment of clear goals and objectives provides a base on which the succession planning process will develop. If the owner is not sure of where he wants to go with the business it will be ineffective and lead to problems in the future.

Items to be included:

a. Owner retirement goals
    - How you plan to spend your retirement
    - How much income you will require to live the life you desire
    - Do you plan to stay active in the business
    - Do you plan to become involved in another business
    - Do you have hobbies or other outside interests to keep you active

b. Family member goals
    - Who from the family plan to stay involved in the business
    - How would selling or transferring ownership impact other members of the family (spouse, children)

c. Goals of other stakeholders (partners, shareholders, employees, etc.)
    - Will partners or shareholders buy you out
    - Does your leaving the business leave a gap in the operations of the business
    - Will key employees continue under the new ownership

d. Goals relating to what is to happen in case of illness or death of the business owner
    - Provisions for how the business is to carry on if the owner is incapacitated or dies

B. FAMILY INVOLVEMENT IN DECISION MAKING PROCESS

This section is important in that by having the family and all stakeholders involved in the decision-making process, or at least kept informed of the decisions being made, will alleviate many of the problems that arise relating to inheritance, management and ultimately ownership issues.

Issues to be addressed:

a. Communication
   - Establish a formal process through which information is exchanged between family members relating to the business
   - Communication is critical, all affected members of the family must be provided with the opportunity to express their ideas and opinions

b. Process for handling family change and disputes
   - Establish a process for dealing with disputes and changes to the family structure which could impact the business such as divorce, death, injury
   - May require the involvement of outside advisors such as a lawyer and/or accountant

c. Family vision for the business
   - A collective vision of what the business is and how it is to operate is necessary if the business is to pass from one generation to the next successfully

d. Relationship between family and business
   - There is a need to be able to separate family and business. Although closely related, it is imperative to be able to objectively make business decisions separate from family decisions.

C. IDENTIFY SUCCESSOR (S)

In this section you will address the issue of who will take over both ownership and management of the business. It must be recognized that these two issues are not the same. This process must not be taken lightly and will require a great deal of preparation and planning.

a. Identification of potential successor(s)
   - It is a difficult process when determining who will take over the business, be it ownership or management. Each potential candidate has to be assessed individually as to

suitability, acceptability, commitment, dedication and determination.

b. Training of successor(s)
   - Once a successor has been selected it is necessary to assess their skills and abilities to determine areas in which training will be required
   - Establish a training plan to bring the successor's skills up to the desired level

c. Building support for successors
   - With other family members
   - With employees
   - With customers
   - With suppliers

d. Teaching successor to build vision for the business
   - Your vision is what has driven the business, under new ownership or management the direction may change and the new owner/manager will need to be able to clearly express the vision to employees, shareholders, partners, customers and suppliers.

D. ESTATE PLANNING

This section of the Plan is exceedingly important, especially if the business owner is planning to retire or is taking a precautionary approach to the future of the business in preparation for being unable to continue operation of the business due to illness or death. Proper estate planning will significantly impact the financial future of the business owner, the business itself and all those with a financial stake in the business (family members, partners, shareholders and employees).

Estate Planning is where outside advisors are necessary to ensure that all necessary issues are properly addressed to maximize benefits to the business owner. Advisors to be consulted include: lawyer, accountant, financial/estate planner and life insurance representative. Each advisor will have their own area of expertise and will be able to provide necessary pieces of the puzzle.

Issues to be addressed in this section include:

a. Taxation
   - Planning for the sale, or transition of ownership of a business can have a tremendous impact in the future of the business. When exiting or transferring ownership of a business, there are potential tax risks and benefits that

only an expert in this field can properly identify. Each business and family situation is unique and must be addressed specifically for that situation.

b. Retirement income
    - Planning for how much money is going to be needed in retirement and where it is going to come from.
    - Based on the owner's retirement goals identified in Section IV. A, lifestyle issues will help to determine retirement income levels required to maintain the desired lifestyle during retirement.
    - Develop an outline as to how money will be saved to ensure a financially secure retirement.
    - Should be done earlier rather than later. The earlier a plan is in place, the easier it will be to make the necessary preparations to ensure that sufficient funds are available at the time of retirement.
c. Provision for other family members
    - Develop estate and personal financial plans for the business owner and spouse as well as the succeeding generation. This will help to reduce the potential for financial problems to be encountered at the time of transition.
    - By addressing the issue of providing for family members in the Succession Plan it will clarify the owner's wishes while all family members can express their concerns.
d. Active and non-active family members
    - The issue of providing fairly and equitably between active and non-active family members is often one that creates family disharmony. Fair and equitable are not necessarily synonymous terms and must be addressed in any estate plan.
    - This issue needs to be discussed and concerns addressed before being finalized to reduce the potential for conflict at a later date.
e. Other financial considerations

- Address any issues relating to financial implications impacted by the transfer of ownership of the business. Unforeseen financial implications can have very negative impacts to the future value of the business, the financial stability of the retiring owner and the salability of the business.

E. CONTINGENCY PLANNING

As plans rarely proceed smoothly or as desired, it is important to consider what could go wrong or awry and prepare alternatives on how to address situations as they occur. It will not be possible to anticipate every situation that may occur, but you can anticipate the more likely scenarios and prepare for them.

A good approach for this section is to look at "what if" scenarios and have a strategy outlined to deal with the situation if it arises. This need not be highly detailed but should be looked as being a guide if unforeseen circumstances occur, such as illness or death of the principal or key person in the business.

A simple strategy may be to prepare a list of possible situations that could occur and from there identify what you would expect to do, or have done. By using this method, it will cause you to look for solutions in advance rather than having to react at a time of stress or duress.

F. CORPORATE STRUCTURE AND TRANSFER METHODS

In preparing for business succession it is necessary to review and update the organizational and/or structural plan for the business. In many small businesses, the owner is the sole person responsible for all aspects of the operations. As this person plans to remove himself or at least reduce the active role they play, it may be necessary to differentiate between ownership and management responsibilities and create positions for these roles.

The goals previously established, followed by the choice of successor(s) will factor into how the business should be structured to the benefit of the owner and the business itself. Just because it worked in the past, the strengths and weaknesses of the successor need to be considered and a structure be established to take full advantage of strengths and compensate for weaknesses.

Issues to be addressed in structuring the business for transition include:

a. Identify roles and responsibilities
    - As you prepare for retirement or selling of the business it is necessary to ensure that current family members and employees have clearly defined

roles and responsibilities to aid in the smooth transition to new ownership and management.

b. Fill key positions
    - Ensure that key management and specialized positions are filled making the business more attractive and prepared for transition. A business with a strong management and workforce is more attractive to potential buyers.
c. Structure the organization based on who is to be the successor
    - Look at the strengths and weaknesses of those to take over and build a structure to take advantages of strengths and compensate for personal weaknesses.
    - Establish roles for family members (if applicable).
    - Separate ownership and management roles if necessary.
d. Take into consideration any potential roles for the retiring owner
    - Advisor
    - Consultant
    - Chairman of Board of Directors
e. Restructuring may be required as the original owner often fills multiple roles that may need to become separated due to skills, knowledge and/or experience.

There are a many methods that can be utilized to transfer ownership of a business either to family members, partners, employees or outside buyers. Each business is unique and must be addressed based on present circumstances. This is best addressed by bringing in professionals to aid in reviewing the alternatives and selecting the method best suited to your needs.

f. Lawyer
    - To examine the legal implications and how to minimize potential conflicts between buyer and seller as well as looking after the interests of family members.
g. Accountant
    - Will assist you in looking at the financial issues aiding in making the transition with as few financial implications as possible.
h. Financier

- Will be able to provide information to you as the seller, which will allow you to make improvements or changes designed to make the financing of the business more attractive to potential buyers.

G. BUSINESS VALUATION

It is important that in preparation for succession of a business that steps are taken to enhance the value of the business in order to make it more attractive to potential buyers while maximizing tax benefits to the current owner.

There are various types of valuation methods used by accountants, realtors and business brokers. It is best to review the options with these professionals in order to select the method best suited to your circumstance.

Some of the factors that impact the value of the business are:

a. What is to be sold?
   - Are the assets of the business or shares to be sold?
b. Where is the business located?
   - A business located in a small market may not have the resale value of one in a larger market
c. Profitability
   - Consideration must be given to the current profit margins and if there is potential for growth. A business that is mature and has limited growth potential is not as valuable.
d. Financing
   - The ability of potential buyers to obtain financing will impact the actual value of the business. Lenders look at value of a business differently than an accountant will, take this into consideration when establishing a sale price as it may provide a more realistic view as to what you can expect to get out of the sale.
e. Inventory
   - The value of the inventory to be included in the sale of the business may form a significant percentage of the overall value of the business. The difficulty arises in placing a value on the inventory that is acceptable to the seller, the buyer and

most importantly to potential financiers. Often financing of inventory is limited or non-existent.

H. EXIT STRATEGY

In this section of the Succession Plan, you will address issues specific to the actual transition of ownership and removing yourself from the day-to-day operations of the business. It involves the comparison of alternatives and a framework for how to make your final choices.

a. Transfer method
   - Selection of the actual method of transfer to be implemented, be it family transfer or sale, sale to a third party or possibly the liquidation of the business are examples.

b. Establish timelines
   - Identifying a schedule for the implementation of the components of the Plan. Without a schedule it will be difficult to meet your goals and objectives.
   - Make sure that timelines are reasonable and achievable.

c. The Exit Plan needs to published and distributed to all persons participating in the succession process.
   - Provides an opportunity for clarification of roles and responsibilities.
   - Provides an opportunity for those affected to raise issues and concerns and bring resolution to those issues prior to implementation of the Succession Plan.
   - Aids in ensuring that owner's wishes are adhered to in case of illness or death.

I. IMPLEMENTATION AND FOLLOW-UP

It will be necessary to review your Succession Plan from time to time. A well-prepared Plan will be done early and will require updating and revision as situations change. As with any strategic planning document it must be dynamic and flexible.

An effective means of ensuring that you take the time to keep your Plan current is to schedule a regular review process. As a suggestion, set aside a specific period each year to examine the Succession Plan and assess its applicability and address any changes that may impact your ability to implement the Plan as required.

V. CONCLUSION

At this stage of the planning process you will be taking a final objective look at all aspects of your Succession Plan and determining your readiness and in many circumstances your willingness to proceed with succession. It is here where you may wish to identify some of the criteria you will utilize in making the final decision to start the process of implementing your decision to transfer ownership of your business.