Succession Planning

Can you pinpoint what is next?

SMITH, KESLER & COMPANY, P.A.

CERTIFIED PUBLIC ACCOUNTANTS
COVERING THE CAROLINAS

Succession planning is:

- a process of identifying and developing internal people with the potential to fill key business leadership positions in the company.

- increases the availability of experienced and capable employees that are prepared to assume these roles as they become available.

(compliments of Wikipedia)

Owners do not just retire:

- Retirement is:
  - reactive, restricted, a narrow approach

- Succession is:
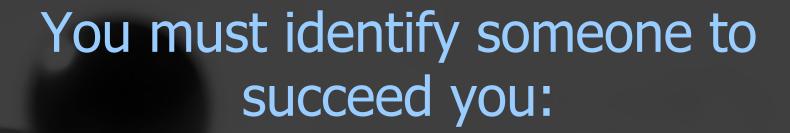 - proactive, flexible, organized and broad

Not this easy:

- Bobby Bonilla: $1.19 million every July 1 for 35 years

- Charlie Weiss: $6.6 million reasons to get fired

- Alex Rodriguez: $20 million to walk away

The baton must be passed

and not always when you expect it

You must identify someone to succeed you:

internally or externally

Types of transitions:

- Asset Sale and/or Industry Roll-Up
- Employee Stock Ownership Plan
- Deferred Compensation Plan
- Stock Sale
- Old Company/New Company
- Gifting

Our focus today:

- ## The Company Perspective:

  - Does the company have to finance the deal?

  - Does it require a dump truck load of cash?

  - Do I sell the assets or the company?

  - Do I sell to employees or outsiders?

  - What is the company worth?

  - What about the bank, bonding and surety?

  - What generation is providing the most value?

Asset Sale

- Assets of the company are sold
- Buyer incentives for tax purposes
- Sometimes can be part of a roll-up
- New owner installs their processes
- Non-compete agreement
- Can be seller financed or cash deal
- Is the intent to simply close the business? Basically a strategic shutdown.
- Sometimes the best option

Employee Stock Ownership Plan (ESOP)

- Stock is "sold" to the ESOP
- Generally takes large amounts of cash
- Old owners are still involved
- Management can remain in place
- Employees take ownership/pride
- Various degrees of financing
- Highly regulated by IRS – must file compliance returns

Employee Stock Ownership Plan (ESOP)

- Bonding considerations:
  - how much cash is removed at initial transition
  - is management team capable
  - increased debt load to old owners
  - overall equity initially goes to zero on paper

Deferred Compensation

- Compensation provided to key employees for purchase of stock

- Generally an agreed upon formula between buyer and seller for compensation and purchase

- Compensation reduces taxable income when paid

- Ownership transition is gradual

- Provides incentive for continued success of the company

Deferred Compensation

- Bonding considerations:
  - what is payout structure?
  - are new owners capable?
  - recording of short-term and long-term liabilities
  - equity is reduced when deferrals are recorded and can be managed

Stock Sale

- Can be key employee(s) or 3rd party
- Buyer may have cash or need financing
- Income taxes = seller wins
- Are you willing to help finance?
- Will you help with transition?
- Do key employees stay in place?
- Generally does not effect balance sheet
- Can be combined with deferred compensation plan

Stock Sale

- Bonding considerations:
  - are new owners capable?
  - starts as a new client

Old Company & New Company

- New ownership starts new company
- Very little start-up cost
- Shared resources during transition
- Original owners liquidate old company
- Jobs are split between companies
- More reporting required (two sets of books)

Old Company & New Company

- Bonding considerations:
  - are new owners capable?
  - starts as a new client
  - old company may guarantee new company for a period of time

Gift To Next Generation

- Generally within family
- Minimal income tax implications
- Long-term plan
- Original owners withdraw funds over time
- Key question – who has 51%?

Gift To Next Generation

- Bonding considerations:
  - are new owners capable?
  - do original owners sign guarantees?
  - how much is required to be left in company?

Quick Review:

- Asset Sale and/or Industry Roll-Up
- Employee Stock Ownership Plan
- Deferred Compensation Plan
- Stock Sale
- Old Company/New Company
- Gifting

REMEMBER THIS ??

The baton must be passed

and not always when you expect it

If something happened to you today, where does the baton pass?