

“One day, my children, all this may be yours...”

Or.....What will happen to the family business when you are gone?

Many business organisations in Europe are family businesses. While the founder of the business creates a profitable commercial enterprise from nothing, and passes it on to the second generation, the challenge is for that generation to continue to make the business grow and to pass it on to the third generation and so on. Sadly, many family businesses fail to survive beyond the third generation.

This article does not address how to grow a business or to make it more profitable. Instead, it concentrates on the strategic issues that apply to all family businesses, irrespective of the country or the market in which it operates. In addition to strategic matters, tax implications need to be considered when carrying out any business planning exercise.

Can / should the business continue to the next generation?

Is the business fit to continue? This needs to be answered honestly – a business that thrived in the past and is still doing well may shortly become outdated due to the products and services it offers becoming obsolete through no fault of its own. Would it be better to sell the business now (or in the near future) and use the wealth to create other businesses?

Is there a viable successor to run the business? Just because a family member is good at running a division of the business it does not follow that he or she will be good at running the entire enterprise. If one family member is appointed to run the whole business will this create an unacceptable emotional strain within the family? Do you want a business that continues to run well, but a family that becomes broken due to internal strife? (Can that strife be avoided or managed – possibly).

Be honest to yourself - What do you, as owner, really want? Do you want to sell the business and enjoy the satisfaction of having created something that has done well and to cash in your prize and deal with the money as you see fit, or do you want all the hard work that you have put in to creating/continuing the family business to be a good base for the continuation of the business? – There is no right answer it depends on what you want.

What does the next generation really want? – Do they feel emotionally obligated to continue in the business because “it is there”, and because it is a family institution, and because it is expected of them, or would they prefer to “do their own thing”? Again this needs to be answered honestly.

If you as owner sell the business, what will you do with your time afterwards? If you hand over the reins of the business, will there be a continuing role for you as a consultant? Can you financially afford to pass on control of the business? Will you be able to cope with being in the business but not running it? If your life is the business, you need to get more hobbies.

If you decide to sell the business

You clearly want the business to be in the best shape it can be, so as to attract a prospective buyer. Therefore all accounts and records need to be well organised and up

to date, debtors need to be chased and any disputes with other parties settled or dealt with. In other words, do the preparatory work so that the due diligence process that a purchaser will carry out will be as smooth and easy as possible without nasty surprises.

If the business is being sold and there are family members working in it, then they need to be agreeable to the sale going ahead and they need to have a plan for what they are going to do for income after the sale goes through, unless they are to be given service contracts or continue to be employed. A business can be sold within the family itself.

Do not forget that running a family business is a skill in itself, and this skill is transportable nationally and internationally. If you are good at running a business it does not matter which type of widgets or services you are selling - it all boils down to the same thing, but of course one needs to be aware of cultural and market differences – however the same principles apply.

If the business is to be kept within the family

Succession planning should not be left to the last minute. It should also not be done too early either as it is difficult to plan for the kids to run the different divisions of the business while they are still attending kindergarten. There is a happy medium. The next generation needs to be educated and trained to run the business or part of it. Just because someone is very good at running a business, it does not follow that they are also very good at training the next generation or integrating them into the business. Family members should not be brought in to positions of power just because they happen to be a member of the family; they should have to prove their worth. Taking a responsible and transparent approach will reduce resentment and claims of nepotism from non-family employees in the business. It is recommended that family members who come to work in responsible positions in the business should have some sort of relevant college or university education, and that they have worked in another business before being brought into the family business; that way the family business will be enriched by the experiences and ideas they obtain outside.

Have a clear timetable; decide on when you as owner of the business are going to step down, whether it be a complete or a phased exit. Also decide on when to start involving the next generation in aspects of running the business. Jumping in at the deep end is only advisable when in a swimming pool, not in a boardroom!

What if the business is not big enough to accommodate the family members who want to run it or be involved? - There are various solutions – the most obvious is that the best of the family members go into the business, and the others do something else – this is easy to say from a distance, but in practice it may just not be feasible. In that case the business needs to grow in order to accommodate the various people and this can be done by taking over another business or expanding the business to create a new division; this would involve a certain element of investment and it could be that an equity investor is brought in to provide capital in exchange for a piece of the action in the form of some sort of shareholding. However, any expansion or diversification must be done solely for the good of the business, rather than being undertaken in order to keep a family member happy.

The family and its expectations

The owners (shareholders/partners) of the business will be entitled to share in the profits by way of dividend or profit share. However, some of these people may also be working in the business, and they will receive a salary and possibly a bonus. It is logical to argue

that if someone is working in the business and they are also an owner then they should receive their full dividend/profit share plus a salary because they are giving of their time and labour to help the business. But there is a contrary argument, which is that the people who are working the business should have a smaller shareholding because they are getting an income from the business, so that all family members get the same benefit from the business. However, the family members who do not work in the business can earn money elsewhere. These different arguments are given to show the diversity of views surrounding family businesses.

Tax implications

Whether the business is retained or sold, it is necessary to consider the tax impact of your actions – the various tax reliefs that are available as well as inheritance tax, capital gains tax, and other taxes. Proper advice should always be obtained from tax specialists. However, as in all business situations, any course of action should be followed because the particular action is appropriate and desirable in itself, not purely because it is the most tax-efficient.

The benefit of having external strategic advisers

A family business has a vast array of good advice available to it to deal with financial, legal, governance and operational matters. But very few businesses consider obtaining advice on strategic matters. It can be highly beneficial to the business to have an external adviser who knows or who can quickly get to know the business well, and who can advise on strategy including succession issues from a detached view point. The adviser should not have any interest in the business whether as family member, shareholder or employee. Thus he can look at the business objectively, and give his views honestly on the basis of genuinely doing his very best for the business. The lawyer is ideally placed to fulfil this role, as he or she is also a business person, and in addition to the experience he or she has in running the law practice, a wealth of wisdom will have been gathered from advising clients of the law firm in the day to day matters affecting their businesses.

CLG – Commercial Law Group

Commercial Law Group is a pan-European group of commercially and practically minded lawyers who meet every six months to exchange ideas and experience, and who work well together on cross border matters. They are all well equipped to handle local as well as international client businesses, and they understand the many factors that are involved in advising family businesses. All members of CLG are approachable and are happy to discuss any matters relating to a business. Details of CLG and its member firms are available on www.clqlaw.eu

Don't delay!

It is very easy for people who are running a business to devote their whole energies to actually running and growing the business. After all that is why they go into work every day. However it is essential to stand back occasionally and to think about the medium and long term future of the business and to plan ahead. This is important for your sake as owner of the business and for the sake of your family. Allocate some time for yourself in the weeks and months ahead to focus on the future of the business, and seek proper advice. You will be glad you did.

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