Host: Do you know what it's like to build a business? You work 24/7 for years just to get a steady income. Then it starts to take off and you hire staff and consultants and professionals to help you. You've got a wonderful supportive spouse and two really great children. You start hitting middle age and your business is hitting its stride. Then those two wonderful children you have, have supported with the business, and have built the business for, they come to you and they say: "Guess what? We don't want your business. We don't want to come into the business." One wants to go into medicine, the other wants to be a teacher, and no one wants to follow in your footsteps. Neither of these ingrates want the family business.

Host: To help up understand what to do next are two experts in the field of succession planning. Murray Gottheil is a partner with Pallett Valo and heads up the firm's business law practice. And Sonia Vaknin is a partner with HS&Partners Chartered Accountants and heads up the tax practice of the firm. Sonia, Murray – welcome to the show.

Host: How often does this happen? Murray – how often does it happen where some poor business owner, they're in there, they're slugging away, they finally get the business working properly and then they find out their children – their 1, 2, 3 children – they just don't have any interest in the business?

Murray: I think it happens all the time. Some kids want to be in the business, some kids don't want to be in the business and the interesting thing is that the parents usually don't have a good handle on it. They very often haven't been speaking to the children and don't really have any idea of what the children want to do.

Host: Sonia, when's a good time to start succession planning for your business?

Sonia: Well, you know we often hear business owners say "I'm going to work until they carry me out in a pie box!" So business owners, as a matter of course, try to push it off and not deal with the inevitable transfer of the business. But when it comes to children, as you were saying, I advise my clients to talk to their children as they go through high school, as they go through university, as they start to think about their careers and what they want to do and be when they grow up. And not push it off or take it for granted that the children are going to come in into the business. Because statistically, less than 10% of all family businesses actually succeed past the second generation.

Host: And why is that? Is it because the third generation runs them into the ground like the Eatons did?

Sonia: Well, I think its most often the second generation that runs it into the ground and that can be either because as you say, the children never had an interest in the business in the first place, or they may lack the skills and the experience. And because succession started later in life, they didn't have the mentoring opportunity under the first generation.

Host: So when the business owner starts talking to their children when they're 4 and 5 years old and they love going to mommy and daddy's office and playing and they think "great! The kids are interested in the business!" and then they never talk about it again, until they find out they're off to university and they're studying teaching and medicine. Murray what's worse – is it worse to have no one interested in the business or to have too many of the children interested in the business?

Murray: That's an interesting question. I'm not sure which is worse. I'm thinking of one of my clients where the kids have been involved in the business, as you described, from 3 and 4 years old. They were there every weekend, starting to hammer nails into wood and working on the product. And now the kids are in their 50s and dad is in his 70s and he's still running the business. One of the sons asked me recently, they said "when is dad ever going to give me a chance to run this thing? He was running it when he was 24! I'm 55 and he won't let me do anything!"

Host: Because the kids don't know enough yet!

Murray: Well, that's right – they don't know enough. And that reminds me of another sort of anecdote of two kids where the dad had passed away and they brought in a facilitator and the facilitator said to one of the children: "We need to decide which of the two sons is going to be the president and take over." The son said "Well, I'm not ready yet." Then he asked the other one who said "I'm not ready yet either." And they went to the mom and said "which one of your sons should be put in charge of this thing?" And the mom said "neither of them are ready." The punchline is that the kids were in their mid-50s at the time

Host: And that certainly seems to be the case.

Murray: Yeah, I think the real issue about succession planning is starting it early and thinking it through and having a plan and doing a realistic assessment. The founders of the business – mom and dad – have certain skills, that's what made the business great. Has anyone done a cataloguing of the skills and figured out which skills the kids have, which they don't, where you're going to supplement the skills. Are you going to get outside non-family members to do it? The important thing is that you can't do business succession on the basis that because you're a family member, you're going to be involved.

Host: Right. Ellen McGregor from Fielding Chemical said it best that: "DNA does not give you entitlement to this business." That if you're going to come into the business, you're going to come in based on the skillset that you have. Sonia, what does a business owner do when they find that neither one of their children, as lovely as they are, have the skillset to actually run the business? So they’ve gone through the professional side of things, they haven’t just figured that DNA is going to give them all the skills that they need and now you have two children that say “Well, I’m ready to come in, I’m into the business, I’m ready to take over.” And now you have to have the conversation with them that, you know what, maybe you are good at what you are doing – you’re a sales guy or you’re an accountant guy – but you don’t have the skillset to run this business. How do they have that conversation?

Sonia:  Well, the first step is if they have the desire – that’s already a good thing. And then you get your management team involved. And this is one of the key communication factors that’s very important is having your core management team involved in the process as well because your current management team may get very slighted and offended when you bring in a successor simply because they are in the right gene pool but they don’t have the experience. So if the children are willing to be trained and willing to learn the business then they can start from the ground and work their way up and develop solid relationships with the existing staff and existing management and really learn the business.

Host:  How prevalent is that, Murray, that’s a good point where the children are coming in, you’ve got a great management team there and lots of people that have the skillset to take over and now the kids are just all of a sudden parachuted in from somewhere and now they’re going to run the business. So that’s an important topic – we’re going to talk about that when we come back from the break. We’ll have more with Murray Gottheil and Sonia Vaknin right after the break. There’s more In Business.

Host:  Welcome back In Business. In the studio we have Murray Gottheil and Sonia Vaknin and our topic today is ‘What to do about the family business?’ There’s no way out – the kids don’t want it, now what do we do? But now we have a situation where the children do want it. Just before we went to break, we were talking about business owners that parachute their children into the business when the business has a great management team. Is there a right way to do that Murray?

Murray:  I think there is. The best example that I’ve ever heard of was in a presentation given by Larry Rosen who spoke about the business succession from his father Harry Rosen. And he talked about his father having been wise enough to appoint a mentor – a senior person in the business who would be responsible for teaching Larry the business from the bottom-up. And as Larry Rosen rose through, he gained the respect of the management team in all the different jobs and capacities that he did. And he spoke about how it important it was that it wasn’t his father. There wasn’t that family dynamic to the mentoring process. And I think that’s probably the best example I’ve ever heard about of how to do it right.

Host:  Sonia, mentoring is a great way. Any other ideas about what you do when you parachute your children in? Because they're going to be faced with animosity from the existing management team if they haven't worked in the business. Even if they worked summers, at least they've got a presence there. But people, what do they need to do to do it right?

Sonia: Well children need to earn the respect of the management team and the staff that have been there for a long time, which often time means that they need to put in the hours and the effort and learn the business in all facets of what there is to do. So if it's a construction business, they can start on the construction side and work their way into management level but gain an understanding and experience of all the elements, all the pieces that come together.

Host: Murray, where does succession planning rank in the overall priorities of a business? When should you start, I think we talked about you should start as early as possible, sometimes even when you start the business you need to start thinking about your exit strategy and what you're doing. Where does it rank?

Murray: Well where does it rank or where should it rank?

Host: Both.

Murray: It ranks as an afterthought somewhere around when your friends start having heart attacks in your mid-50s. That's where it ranks. Where it should rank is it should rank on day one because there are things you can do even from a tax perspective on day one that you can't do later. If you're trying to, for example, multiply capital gains exemptions, you want to have other owners involved to be able to do that from the beginning. But more importantly, a business succession involves value. And you build a business by making, and you build corporate goodwill as opposed to personal goodwill, by creating the value right from the beginning – making that business run independently of the owner. So both from the perspective of increasing the value of the business and from the perspective of having that business be in a situation where somebody else can run it, you have to start organizing and planning your business from the beginning.

Host: And that becomes an important part even when you're talking to bankers and financers – they want to know that there is a plan B in case you don't make it all the way through or if you do make it all the way through to retirement they want to know that there is a plan B. So having that succession plan for bankers and financers – it's an important piece of documentation. Sonia what are some of the tax implications or tax considerations that people should look at when they're forming their succession plan?

Sonia: Well where I start with my clients is from a personal, business, legal, tax perspective and sort of in that order. Because you first want to discuss within the family unit, within your management team the personal and the business direction – where the family wants to go. What you want to do then from a tax perspective is you overlay the business plan, the personal plan, with the tax and family trusts give you a great, as a planning tool, flexibility for the future. For example, when you're not sure if the children are going to take over the business or not, family trust buys you time, a lot of time, to be able to come to that decision one way or another. So family trust is very important. They also give you the opportunity to multiply, as Murray said, the capital gains exemption. So, for instance, if you have four family members involve in the business, or not involved in the business but as beneficiaries in a family trust, then you can potentially get up to 3 million dollars of proceeds from a sale of the business – tax free. That's 3 million dollars tax free from just 4 family members.

Host: That's huge. Murray, what are some of the mechanics that you go through to set up a family trust. We hear a lot about them and we think that there's a big bill coming along here somewhere, you know the accountants and the lawyers are going to have to get together on this one.

Murray: You're saying that like it's a bad thing!

Host: Well it's not a bad thing from your perspective – I know that! And we've got to take a little bit of a break. When we come back we're going to talk about some of the things that you could do in a family trust and we're going to talk about some of the best practices when it comes to succession planning. We'll be back with our guests, Murray Gottheil and Sonia Vaknin right after the break. There's more In Business, lots to talk about, there's no way out, sometimes, of a business. But our two experts are going to help you figure it out.

Host: Welcome back In Business. In the studio we have Murray Gottheil and Sonia Vaknin and our topic today is what to do when no one wants the family business. There's no way out of this but we do have some experts on the panel that can help us understand what to do. In succession planning in general and in family trusts, what are some of the best practices that businesses should put in place, Murray?

Murray: I think the first thing is for business owners to sit down and figure out what works from a family perspective. You don't start your business succession planning with a tax plan. You start by looking at your family and deciding what is good for the family and what is good for the business. What skills do the children have realistically? What is it that mom or dad is doing in the business that is going to be missing when the kids take over? Maybe the kids can carry some of the functions but not other functions. What does the family need? Do the parents need the money out to live on or can they afford to say "here – play with it – we've got enough assets outside of the business to support us comfortably throughout our retirement." So there's a lot of questions and a lot of valuation and thought process it has to go through. I think the next important step is to figure out what's this family dynamic like? Can mom and dad talk to the kids about this type of thing or should there be a third party expert facilitator – somebody with soft skills? Now I know Sonia can do this, but most tax lawyers and tax accountants and corporate lawyers can't do it. There are experts out there who can help families talk to each other and do this type of planning.

Host:  And sometimes that's what you do need – you need a third party to come in. And Sonia I know you've done this with your clients. Help us understand some of the train wrecks that you've seen and how you've helped them work through that.

Sonia:  Well a common train wreck situation is sibling rivalry. When you have three or four or five sometimes children, which we see less and less these days, but there are big families believe it or not, and only one or two may be active in the business and the parents as part of their overall estate plan are looking at may or may not be considering estate equalization and "what if I leave the business to these one or two children?" And then you get, as I said, sibling rivalry. So what I try to do in those circumstances is communication. Sit around the board room table, have the parents explain to the children exactly what is that missing link – why does Peter get to be the President and why are you the manager in charge of X? That's all very important. Communication is key. If children understand why their parents are going down a certain path or making the decisions that they're making, then it makes the transition much more smooth and chances are that it will succeed.

Host:  Do you recommend to clients that perhaps they have their children apply for the job just like they would have anybody else apply for the job? Does that make any sense at all?

Sonia:  It probably makes sense. Have I ever actually seen it? No.

Host: So it if makes sense then they're not going to do it!

Murray:  I think if you're that late in the process where you're already talking business succession and the parents are older and you're talking about having the kids apply for the job, it's already too late because they haven't had enough involvement in the business up to that point.

Host:  You've made a good point Murray when you're talking about the valuation of the business and how much money mom and dad might need out of the business. That's got to be an interesting point when the kids have worked in the business, they're coming up, they're getting ready to take over and then they find out that they have to pay for this business! How does that work?

Murray:  Well sometimes they just can't afford to do it. And it's interesting – there are people out there though who run equity funds who might come in and be partners with the kids. That's one possibility

Host:  Larry Klar from Argosy (16:34) has been on the show a couple times talking about that program.

Murray:  That's right. But apart from that, now you have to look at that business and say "have mom and dad done a good enough job making that business independent of themselves that the banker is going to say fine we'll finance the kids because we know that this business is not entirely dependent on the presence of mom and dad." If they've done a great job of that, then they can afford to sell to their kids. Otherwise, they may not be able to afford to sell it to their kids.

Host:  Does it work well when the whole transaction is treated like a business transaction? Is that a better scenario, rather than getting the DNA and the bloodlines all mixed in there and the emotions?

Sonia:  A transaction such as this should definitely be treated as a business transaction but you can't lose sight of family dynamics, family culture and the communication that's involved – the greater communication that's involved, not just with the children and the family members but also with the management team. So there has to be greater communication and a longer time period for everybody to gain to experience, to gain the respect, and to transition the business so that it's not all dependant on mom and dad. So that the customer relationships, the supplier relationships all transition as well, otherwise, as Murray said, the business really has no value.

Host:  That's all important as well – that unfortunately, how old we get and how old our children get, we always think they're still the kids. And, you know, 40 and 50 years old and, you know, they're never going to have the same business relationship with Sam and Terry that we had. And they forget to transition those things. We've got about a minute left. In ten seconds, what's your best advice for succession planning, Murray?

Murray:  Start early, get professionals involved, realize it's a multi-disciplinary endeavour and it should be looked at from a lot of perspectives and if you're the entrepreneur founders who have always run everything and done everything your way, get out of that mindset.

Host:  Get over it – Sonia, your best advice?

Sonia:  I would say be realistic, have a plan A and a plan B in place so that if the kids don't work out as a succession plan, you can always go to a third party purchaser or a management buyout and keep more of the wealth in the family that way than risk ruining the business and running it into the ground.

Host:  Absolutely! And we're out of time. Special thanks to my panel guests Murray Gottheil of Pallett Valo and Sonia Vaknin of HS&Partners.