

Family Business Law

Successful Succession

Recent Canadian studies have found that only 30% of Canadian family-owned businesses make it to the second generation, and only 10% make it to the third generation. This should come as no surprise when viewed in conjunction with results from the 2005 Canadian Federation of Independent Business member survey that indicated that two-thirds of respondents did not have formal succession plans despite the fact that 70% of the owners intend to leave their businesses within the next 5 to 10 years. They say that “people who fail to plan, are planning to fail”. Let us help you plan to succeed instead.

A Comprehensive Approach

Successful succession of a family-owned business requires a comprehensive approach that gives proper weight and consideration to all stakeholders. The owner-operator often defines value and success differently than his or her spouse, children, management and employees. It is essential to align the vision of the owner-operator, so far as possible, with the interests and expectations of the parties the owner-operator will rely on to realize that vision. In those cases where the competing interests of stakeholders cannot be aligned, proper communication, understanding and tactful management of all parties' objectives are vital to preserve relationships and avoid expensive and disruptive conflicts during the formation and implementation of the succession plan.

Leadership transfer is often the most contentious issue facing family-owned businesses, especially where a generational transfer is the desired succession plan. It is often the case that the children of the owner-operator expect to be placed in roles or positions which do not match their individual skills and qualities. In such cases, the owner-operator must assess what role their children can realistically play while being mindful of such children's expectations and feelings. A contrary scenario commonly occurs where members of the second generation have been running the business for some time (with or without the help of qualified managers and professionals) and the original owner-operator is unwilling to address the need for a succession plan and the formal transfer of control.

These issues are emotional minefields, which require a proactive and sometimes formal approach to the communication between family members. At a minimum, the interested parties should have an opportunity to express their visions and expectations before determining

successors and embarking on a strategic plan for leadership transfer. With the assistance of a trusted professional to mediate the discussion, this could be as easy as holding a family meeting. Sometimes, a more formal communication plan is required. An example of such a plan is a “Family Charter”, which sets out a united vision for the business and rules for resolving family disputes. For larger and more complicated businesses, an outside advisory board may help to ensure objective decisions are applied when conflicts arise.

Knowing Your Options

There are a number of options available to business owners who are beginning to contemplate an exit strategy, and each has its benefits and drawbacks. Many owners consider family transition to be the preferred option as it provides a legacy to future generations who have some knowledge of the business, the industry and the owners' vision for the future. Since children often do not share the same interests and values as their parents, and may not have the expertise that comes with years of operating the business, the parents/owners should be able to rely on their professional advisors to provide an objective analysis of the potential for a successful family transition.

Other options include management buy-outs, and selling to unrelated parties. The management buy-out is an appealing option because the owner can be confident that the business will be left in the hands of trusted people who have existing relationships with customers. The negotiation and implementation of a management buy-out requires finesse in order to achieve fairness while maximizing value for the owner in light of existing relationships and loyalties. Selling to unrelated parties also appeals to owners as it provides certainty and finality. Sound advice, attention to detail, an up-to-date valuation and strong advocacy are crucial when

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dealing with unrelated parties, as sophisticated buyers will vigorously review business records and the company's history to ascertain the value of their investment.

Start Early

Succession planning is a process which benefits from foresight and planning. There are a number of stages to succession planning, including clarifying and documenting intentions, identifying successors or buyers, training successors, and transitioning to new management. As a minimum, owners should begin formalizing their succession plan 5 to 10 years before their intended transition and exit.

Legal guidance is required throughout the process of succession planning for: family communication and conflict resolution at the plan's fruition; corporate reorganization

and the use of shareholders agreements, trusts and holding companies to ensure proper implementation and a tax-effective change of control; and proper estate planning, including Wills and Powers of Attorney, to ensure that value is protected and enjoyed by the intended persons into the future.

We're in the Family Business®

Successful succession of a business is one of the most important issues facing business owners today. With decades of rich experience in corporate, estate planning and conflict resolution, the Family Business Law Group is uniquely qualified to guide clients through the succession planning process, which is essential to the well-being of clients and their businesses.

Pallett Valo LLP Family Business Law Group

At Pallett Valo LLP, client service is a family affair. We have been there for many of our clients since the beginning, and have witnessed their businesses grow and evolve. We have seen their children become adults, and take part in the family enterprise, or find their own path, and throughout we have provided our clients with the peace of mind that comes with sound, objective advice to guide them through important decisions.

The Family Business Law Group provides clients with the best advice and guidance on many issues facing family-owned businesses, including:

- Succession planning;
- Acting for purchasers and vendors in the sale or purchase of businesses;
- Implementing estate freezes and other corporate/estate planning strategies;
- Corporate organization for effective creditor and tax planning;
- Resolution of disputes involving shareholders, directors, and management; and
- Facilitating partner, shareholder, and family member buy-outs and reorganizations.

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This article provides information of a general nature only and should not be relied upon as professional advice in any particular context. For more information about Family Business Law, contact a member of our **Family Business Law Group** at 905.273.3300.

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