Planning Your Succession

The future of a business can be particularly tricky when there is no succession plan. Here are some tips for both the transition and transaction of moving on from your garden center.

By Chris Cimaglio

While attending an industry succession planning seminar last summer, we were surprised when a young man stood up and said, "What if the current leadership [his father] doesn't want to get out of the way?" In a group discussion afterward, we commented how lucky that owner was to have someone waiting in the wings wanting to take it over — even though it was clearly a frustrating situation for the son and could be disastrous for his father. The topic quickly changed to: what about family-owned businesses (a hallmark of the lawn and garden industry) that do not have a next generation to take over?

If there is no family to take over the reins, then the logical choices are to transition the business to new leadership and/or your employees (often through an Employee Stock Ownership Program, or ESOP), sell the business outright or simply close up shop when ready to retire. Since a business can often represent about 80 percent of an owner's net worth, we will address the more wealth-saving and positive options of transitioning and/or selling the business.

According to the PWC Family Business Survey, 48 percent of business owners don't know how to or have even thought of preparing for the sale of their company.

What is clear is that the best business transitions begin early and have a team of people working in tandem to maximize the value of the business and get your business transition ready.

The Challenges

"By failing to prepare, you are preparing to fail." — Benjamin Franklin

The numbers are staggering.

Ten thousand Baby Boomers hit retirement age every day, and 60 percent of all business owners are over age 55. According to recent surveys by the Exit Planning Institute, PNC Bank and Kent State, 80 percent of business owners have no transition plan, or have not documented or communicated a succession plan.

Furthermore, 80 percent of these businesses simply are not saleable, nor do they have a proper talent or family pipeline to continue. Of the remaining 20 percent that are sold, 12 percent will be lower than the original asking price.

The study also discovered that 40 percent of business owners did not have a plan that covers their forced exit (death, disability, divorce or illness).

Even though 98 percent of business owners feel succession planning is important, they rarely have a plan in place. When they actually do have a plan, there are several reasons why they don't succeed...

- Many think it is not important and choose to focus on the transition, rather than the *transactional* nature of a business.
- Potential future leaders and family leave the company looking for greener pastures. Owners simply do not adhere to the plan, and many continue to stay long past their expected date of departure (as illustrated by the frustrated son above).

- New leaders are ill-prepared to take over or simply do not perform to the level of the original owner.
- A focus on the past or a mindset fixed on, "This is the way it has always been done," not only cripples future leadership, but puts the entire future of the business in jeopardy.
- Politics, time, lack of commitment and fear.

Successful, Succession Planning = Transition Ready

Not all hope is lost. We have been a part of many succession plans that have been and continue to be successful, and they all share these characteristics...

- The understanding that effective succession planning is more than just transitioning to new leadership; there are transactional components at work as well. They take an objective investor's approach to looking at their business ... *Is the risk at a low level and is there a potentially high ROI?*
- Operational Efficiencies: *Are there efficient processes and procedures in place that can be easily managed and communicated?*
- Financial Strength: *Looking at the metrics (ratios, receivables, banking situation), is the company operating at a high level and doing more with less?*
- Transition ready: *If the owner should suddenly leave or pass away, how easy would it be to transition to new leadership or potentially sell the business for a high return? Legal and financial preparation?*

Transition-Ready Businesses are More Valuable

Transition ready means that you are prepared legally and financially, but also emotionally. We know from our own experiences, especially in a family business, that it is often an emotionally charged and difficult exercise. In fact, according to the Exit Planning Institute, after transitioning or selling their businesses, owners "profoundly regretted" it after just 12 months.

There are some that can just walk away but many more that can't, so this needs to be considered when selling your business. Perhaps it is an earn-out or a situation where you ease out of the business over time, and this would need to be a part of any discussion with new leaders or buyers.

Operational discipline and financial strength, looking at the business from an investor's perspective, all point to higher success rate. Here are some other value builders that will not only increase the valuation of your business but will make it infinitely more valuable in the eyes of an investor of buyer. This is primarily what they look for:

- **Presence of Recurring Revenue:** Consumables, which are usually always present in a lawn and garden operation; loyalty programs and subscriptions; sunk money, for example, long-term landscaping contracts or recurring purchases, such as lawn care programs; and leases.
- **Consistent Sales and Profit:** The ability to drive revenue but not at the expense of margin. New product/service offerings, new markets, diversification and those elements of your operation that deliver consistent sales and profitable results.
- **Owner Independence:** Can the business operate independently of the owner? Workaholics, who are in their operations seven days a week and micro-manage their businesses, are bad bets for a potential buyer.
- **Sales and Marketing:** An owner that has all of the key relationships and is responsible for a majority of the sales, especially to larger customers, can be an issue. Are customer relationships spread out among your staff? Are you staying on top of trends? Website, eCommerce, email lists, social media are all critical for today's garden center.
- **Barriers to Entry:** Are there any governmental hurdles? How established is your customer base? Essentially, what potential buyers are looking for here are barriers to entry for potential competitors. Location is a critical factor as well — your proximity to your customer base, and is a competitor angling to move into the area?
- **Do You Have a Niche?** A differentiator or something you are known for in the community? Is the niche side of the business growing above average?
- **Strong Modernized Systems:** Do you have up-to-date POS systems, and are your processes and procedures efficient? Is the information readily available?
- **Bankability:** Well-prepared financials, key performance metrics with predictable and reliable cash flow.

Transfer Ownership to Employees or an Outside Buyer?

ESOPs can provide a variety of tax benefits for ownership as well as the non-family employees that would want to see the business continue into the future.

According to the National Center for Employee Ownership, "ESOPs are most commonly used to provide a market for the shares of departing owners of successful closely held companies, to motivate and reward employees, or to take advantage of incentives to borrow money for acquiring new assets in pretax dollars." Although sometimes the cost may be prohibitive in setting one up, there are major tax benefits of having an ESOP, especially for an S or C-Corp.

Another option may be to have your existing company leadership buy you out. For both the ESOP and buy-out scenario, whether to employees or an outside buyer, it is critical to have a team of knowledgeable advisors (your financial planner, attorney, CPA and other key advisors) on the same page to make sure you are financially and legally ready.

A glut of garden retailers and other companies will be transitioning or be up for sale in the foreseeable future as the Baby Boomer generation continues to move into retirement. Focus on making your company more transition ready and those aspects of your business that drive and build value.

It is also important to focus on your emotional readiness with a life or business coach. There is a lot of value in aligning yourself with a well-trained executive search and business advisory group that can help you find your next leader and management team, as well as help you build your organizational bench strength. Instead of planning to fail, we can now plan a clean transfer and a mutually beneficial transition or transaction to a new owner.

It is hard to transition when there is no family in place to take the reins but that doesn't mean that the planning should stop — it is more important than ever to get started.

After all, succession planning is about preparing for the transition or transaction of your life. Are you ready?

Sources: PWC Family Business Survey; PNC Bank; Kent State; Exit Planning Institute; Pew Research Center; and the National Center for Employee Ownership.

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