TWP

A Guide to Succession Planning

Business owners and leaders are often focused on the day-to-day running of their company but they also need to keep an eye on the future.

At some point, every director or partner has to step down and hand the reins to a successor, which is why it is important to have a clear succession plan in place.

> “Succession planning is the procedure used to identify and develop a business’s future leadership team, which must consider how a business will fill critical roles, including who may one day own and run the business.”

Although the main aim is to consider how a business will gradually fill key roles effectively, it must also look at emergencies, such as the death or long-term illness of a director or partner.

Even businesses with a young leadership team in place should have a structured succession plan prepared so that responsibilities within a business can be assigned efficiently, talent developed and tax liabilities reduced when the time comes.

A structured succession strategy

While many owners may have a general idea of who they would like to run their business in future or how it should be run, without a formal plan in place it can be difficult to put the necessary steps in place to facilitate a smooth transition of power.

Depending on the candidate(s) you choose, it could also take years to develop the skills and experience needed by a new owner or leadership team, which is why having a clear plan and timeline in place helps to prepare the business for succession.

> “Having a structured succession plan in place also helps you to prepare your customers and suppliers for the new candidates, ensuring you can maintain relationships that are integral to your company.”

A succession plan also considers the finances of your business. In some cases, a business may need to finance the transfer of shareholdings to the new team or a business may see this as a point to invest in new services and products to maximise the impact of the succession.

Owners themselves also need to think about the tax implications of selling their shares in a company, as it may make sense to have a more gradual transfer of the shareholding to reduce the personal financial impact on a director.

This why it is strongly advised for all businesses to have a formal, structured succession strategy in place, especially if members of the current leadership team intend on leaving the business within five to 10 years.

Starting the conversation may be daunting, but the sooner the work on your succession plan begins, the better prepared your business is for all scenarios.

Why you need a succession plan and what the benefits are

Without a succession plan, your business could find itself without effective leadership once you have decided to retire or if you suddenly had to leave the business for an extended period.

Without a plan there could be a substantial impact on the viability of your business and the relationships that you may have forged with clients and suppliers should you need to leave the company.

Having assisted a wide range of firms from a variety of sectors with their succession plans here are some of the benefits that we have uncovered.

Developing future leaders

When you commit yourself to create a formal succession plan it requires you and your company to identify and then develop future leaders within your business or find suitable outside candidates.

This is a crucial part of preparing your plan and one where you could fall at the first hurdle.

If having reviewed your business you can find no suitable candidates then you need to consider your options.

Do you:

- Train and upskill existing team members
- Hire in new talented senior staff members
- Seek external support for a new management team

Each approach certainly has its merits and your choice could be entirely dependent on your situation and plans for retirement.

For example, if you decide you want to leave the business in three years you may not have time to train and develop internal candidates, in which case, you may need to consider an external hire or bring in a consultant or temporary leadership team to give internal candidates the time to upskill.

Many businesses tend to favour training and developing internal talent, but this can be costly and is not without risk, especially if that person decides to use their new skills to seek work elsewhere.

Maintaining relationships and brand identity

A big challenge with any succession is maintaining those hard-earned relationships with your clients and suppliers.

> “It can take years to nurture these connections and by leaving a business it could sever ties that are difficult to then repair or replicate.”

Many businesses also derive a large part of their reputation and brand identity from their team of directors.

You only have to look at the likes of Elon Musk or Sir Richard Branson to see the positive (and sometimes negative) impact of having a recognisable CEO.

Even at a local level, your business may have built up a strong reputation based on the approach of your current leadership team, which would be difficult to replace without prior preparation.

By allowing candidates time to make these connections, prior to an owner or key person’s retirement, can make a considerable difference to the future success of a company.

An extra pair of hands

Beyond the eventual handover of the business to the new team, ensuring your managers have the skills to be able to take up more senior roles can have many benefits.

By upskilling candidates, you can ensure that the expertise within your company isn't concentrated purely at the upper levels.

This can give you the freedom to let others work autonomously, while you focus on other areas of the business and its growth.

It also ensures that there are others in the business with a keen eye on the critical processes who can spot where issues may arise or take advantage of new opportunities that may come your way, which can help your company to thrive.

Business continuity

One of the scenarios that few business owners want to consider is what would happen if they were affected by a serious long-term illness.

Even young business leaders can be struck down without any prior warning and so having a plan in place will help to give you some peace of mind.

Within their succession plans, owners also need to consider other key people in the business and have plans and built-in redundancies just in case that staff member has to leave the business.

A sudden event such as the departure of a key employee can have a big impact on a business and its plans – so it is important to have succession steps in place to deal with this.

A clear vision for the future

When you and your senior managers have a clear vision for the future it is easier to plan and put the necessary resources in place.

Every business should include a structured succession strategy as part of its wider growth plans.

By ensuring that you have plans for the future it is easier to make the transition seamless and it will ensure that your company grows with intent, instead of wandering aimlessly into uncertainty.

> “Other benefits to succession planning may include providing help in ascertaining which areas require innovation and setting realistic goals for growth.”

This can help to ensure that you have the finance and skills you need to continue operating.

Alternative approaches

You must decide on the arrangements that are the most advantageous for you and your business. It may be helpful to have more than one option at your disposal so you can react to different scenarios.

Popular options include:

Keeping it in the family

Many business-owners elect to pass the business on to a relative(s), particularly if they are already involved in running a business. This may give you peace of mind that you are handing the company over to someone who has the commitment and knowledge to carry it forward. Although it is important to remain objective and ensure that emotional considerations are balanced against the company's prospects.

Management buy-out

This is when the existing management team buys the company from the present owner.

Management buy-in

A management team from outside the company buys the business and becomes the new management.

Full sale

The company is bought by a third party, although the existing management team remains in place.

Buy-in management buy-out

This has elements of both a buy-out and buy-in. The new owners will include members of the existing management team and individuals from outside, who join that team once the transaction is completed.

What you should do to prepare for this

Depending on the nature of your business and the number of directors or partners involved in the running of the company there are several ways to prepare a business succession plan.

In many businesses, it may help to put together a succession board or committee made up of directors and shareholders, as well as outside professionals such as your accountant, to consider what steps need to be taken.

They should establish what approach for succession needs to be taken, outline an action plan and put in place the necessary changes for the transition to take place.

What a good plan should include

Many things need to be taken into account when you start to think about a succession plan. The decisions that need to be taken will vary greatly depending on the size of your business, the sector you work in and your circumstances.

Not everything will be relevant to your company, but it is important to be thorough and make sure that you have considered all of the key points.

Here are a few questions to ask yourself before preparing your plan:

How will the succession plan impact on your employees, customers and suppliers?

If you are not a sole owner, how will any plans affect your fellow shareholders and directors?

Who needs to be involved in any decisions that you make?

What changes will the transition bring to your business? (thinks about location, staffing, company name etc.)

Have you considered a successor?

Do they have the skills?

What is the timetable for the transition and how will it happen?

Who do you need to consult about the process?

Have you done a risk assessment and due diligence?

The different approaches you may choose to take when exiting a business could have a big impact on the plan you create. However, all plans should include the following:

- A timeline for succession
- Actions that need to be taken prior to and after succession
- Business continuity following an unexpected event
- How shares are to be transferred
- Potential candidates for succession
- Specific policies or rules related to the succession

At some point nearer to the transition you will need to consider either changing or creating the following:

- A business or share sale agreement
- Business licences
- Finance agreements
- Name changes
- Outstanding contracts and agreements
- Share transfers

You may wish to outline the process for making these changes within the plan itself, just in case, something should happen to the key person's responsible for these documents or shares.

Determining a successor

Succession planning, particularly when considering internal recruitment, relies on a formal and informal development process.

> “A key part of any preparations for succession is talent management. This covers a wide range of activities designed to attract, recruit, identify, develop, engage, retain and deploy talented individuals both internally and externally.”

While many businesses may prefer to select their candidates for succession internally, there are many valid reasons to recruit externally, especially at senior levels, such as bringing new skills or approaches to an existing business.

Within larger groups of businesses, it may also be worth considering a lateral move through secondment from another part of the group.

A sideways move into a different job, perhaps even without any additional compensation, may be an alternative way of gaining additional experience or skills quickly without the costs or risk of an external hire.

Identifying suitable internal candidates can be done in several different ways, but more formal techniques such as performance reviews and assessing competencies can be a good way of finding a candidate that is the right fit for your business.

When it comes to external hires it may be beneficial to employ the services of a recruitment agency or ‘head-hunter’ to find a person with the right skills and mentality to take on the role required.

Moving on

When an owner leaves a company there are various ways for them to move on.

Some favour a complete split from the business, whereas others prefer a managed departure over several years to ensure the business is in good hands.

Similarly, how shares are disposed of may differ. In some cases, an owner may wish to dispose of their shares all at once, whereas others may structure the disposal of their shares over time – especially where it offers a tax advantage to them.

Capital Gains Tax (CGT) is a big consideration during the succession process, as an owner is likely to be taxed on the disposal of their shares.

> “Although Business Asset Disposal Relief (formerly known as Entrepreneurs’ Relief) can help to cut the CGT rate from 20 per cent to just 10 per cent in some cases, there are additional benefits from disposing of assets over multiple tax years, which directors or partners may want to consider.”

To ensure a clean break, the new management team or owners may want to consider how power is transferred and the role that the departing team will take after they leave.

As you can see, there is a lot to consider when preparing a succession plan. The points covered in this guide cover the succession of most regular businesses, but there may be additional problems to contend with in certain circumstances, such as family businesses, that may require owners to think about the Inheritance Tax implications of handing over a business to a relative.

How we can help

At TWP Accounting, we have assisted a wide range of businesses with their succession plans.

Helping them to assess the impact on their finances, acquire additional funding and consider the tax implication of passing on a business or shares.

Working with our many close partners, we can also help our clients look into the legal implications of succession and put steps in place to achieve a successful transition, whether it takes place over a single or several years.

To find out how our team of tax, business and accountancy advisers can help you put a successful succession plan in place, please contact us.

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