SUCCESSION PLANNING

From one generation to the other

Text Stephen Evans — **Illustration** Myriam Heinzel

EMOTION AND FINANCIAL CONCERNS clash when entrepreneurs think about succession planning. Whether they expect to pass the firm to children or to sell the business, it can be hard to be clear about goals and take a dispassionate final decision.

Some entrepreneurs are able to work until they drop, but most eventually have to face tough choices about succession. Passion, ambition, and personal identity are invested when building a business, and these emotions need reconciling with financial concerns. An exit strategy needs careful planning if the business's legacy and a life's work are to be preserved. "*We advise our clients to start the discussion years before the planned exit date*," said Daniel Schneider of mergers and acquisitions advisory firm Tenzing Partners. He reckons that buy-out deals generally take 6 to 12 months to plan and carry out, and substantial prior discussion and preparation is needed.

When passing the company to the next generation, the first step is to gauge which or how many of the children have the aptitude or experience to take over. Alternatively, senior managers might be in the best position to ensure continuity and inject fresh enthusiasm. Another option is to sell to a competitor, domestic or internationally based. This will come with mixed emotions. On the one hand it's flattering to know the business is in demand, on the other it can be tough to see one's life's work swallowed up.

ESTABLISHING A VALUATION

Establishing a widely accepted valuation is a key early step. Entrepreneurs may have an inflated idea of the company's worth, while potential buyers will of course want the best deal, so hard numbers help focus minds. There are several established, accepted techniques for taking a dispassionate view, with assessments made studying past earnings and the business outlook. These can be bolstered with comparative valuations using the financial figures of publicly listed market peers, and recent acquisitions of similar quoted companies.

Mr Schneider adds that these figures can only be taken as a guide, as private companies will generally trade at a discount due to these shares not being available for sale on the open market. Of course numbers don't tell the whole story, and they need to be assessed in the light of the market and the individual business. Businesses with a clear path to further growth will command a higher valuation.

"*If planning starts at an early stage before a transaction, this is also an opportunity to take a fresh look at the business's strategy and see if there are ways to increase the future sale price*," commented Mr Schneider. "*This review might suggest the company could benefit from an intermediate step via growth through acquisition, through an alliance, or organically. Alternatively, there might be need for rationalisation or divestment*," he said. These ideas may clash with the expectations of the ownership, who may seek a second →

opinion or they may trust their gut instinct. However, Mr Schneider is convinced a dispassionate analysis is a necessary part of forming a firm view.

REACHING A DEAL

With a valuation in mind, hard-headed discussions can begin in earnest with interested parties. If a transmission to the family is planned, the entrepreneur and their children will need to decide who will have an executive, supervisory or a passive role. Alternatively, a child might wish to take the cash and play no future role in the business. If the entrepreneur is looking to sell, a management buy-out might be the best way to guarantee the continuation of the company's values. Alternatively, a private equity fund or an international business seeking substance in Luxembourg might be the way to maximise returns. Ideally there will be a solution that balances business values and financial gain, so it will be necessary to tap into international buy-out networks to find the right buyer.

Once the broad strategy is agreed, then direct approaches can be made to potential buyers. These discussions should be covered by a non-disclosure agreement as initial interest is probed. Then if there is tentative interest, a non-binding letter of intent can be issued with a favoured party, leading to a full due diligence process. All the books will be put on the table as the buyer checks the firm's credentials. If all goes well then a binding offer will be made, which will evolve as details on price, structuring, timing and post-transaction integration are discussed.

ASSESSING THE POTENTIAL

Few entrepreneurs have the breadth of expertise to handle this range of challenges. Hence Mr Schneider is convinced of the importance of having a team of trusted advisors who can walk the entrepreneur through the financial, technical and emotional challenges. Banks, lawyers, notaries, auditors and consultants can all handle some or all of these tasks. "*When considering a succession, it is often necessary to have a neutral trusted advisor to take the heat out of the situation,*" commented Mr Schneider. "*It helps to have someone who can work with all interested parties and make a sober assessment of the situation,*" he added. When a decision is made, this has to be communicated, and often this will not be welcome news for some, and the advisor could help shield the owner. Sometimes the owners will need protecting from themselves. They may have an over-inflated view of the company's worth, but a dispassionate assessment could save heartache and result in the most lucrative settlement.

There have been concerns in recent years in Luxembourg that a younger generation have been less willing to take over the reins of family businesses. The high remuneration and regular hours of jobs with the state or the financial sector are appealing. However Mr Schneider thinks things have changed. "*We've definitely seen a shift of attitude in recent years,*" he noted. "*Entrepreneurship has become sexy, and there have been some high-profile examples of children taking over and transforming traditional companies.*" This has generated favourable press coverage, and encouraged young people to take the riskier but more rewarding path.

As well as greater demand from the younger generation, Luxembourg's status as a cross-border business jurisdiction means there is more interest than ever from international purchasers. In short, these are good times for entrepreneurs considering making timely plans for the next phase of their lives.

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