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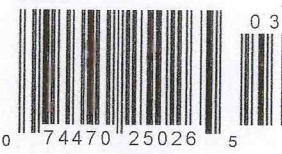
HOW DO YOU KEEP BOTH THE FAMILY AND BUSINESS INTACT?

AMINY AUDI AND GREG HARDEN TALK ABOUT THEIR COMPANIES AND THEIR SUCCESS OF RUNNING A GENERATIONAL FAMILY BUSINESS.

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Generational Transition

CNY Business Exchange asks three family/generational business experts to identify the most common generational transition issues that family businesses face today.

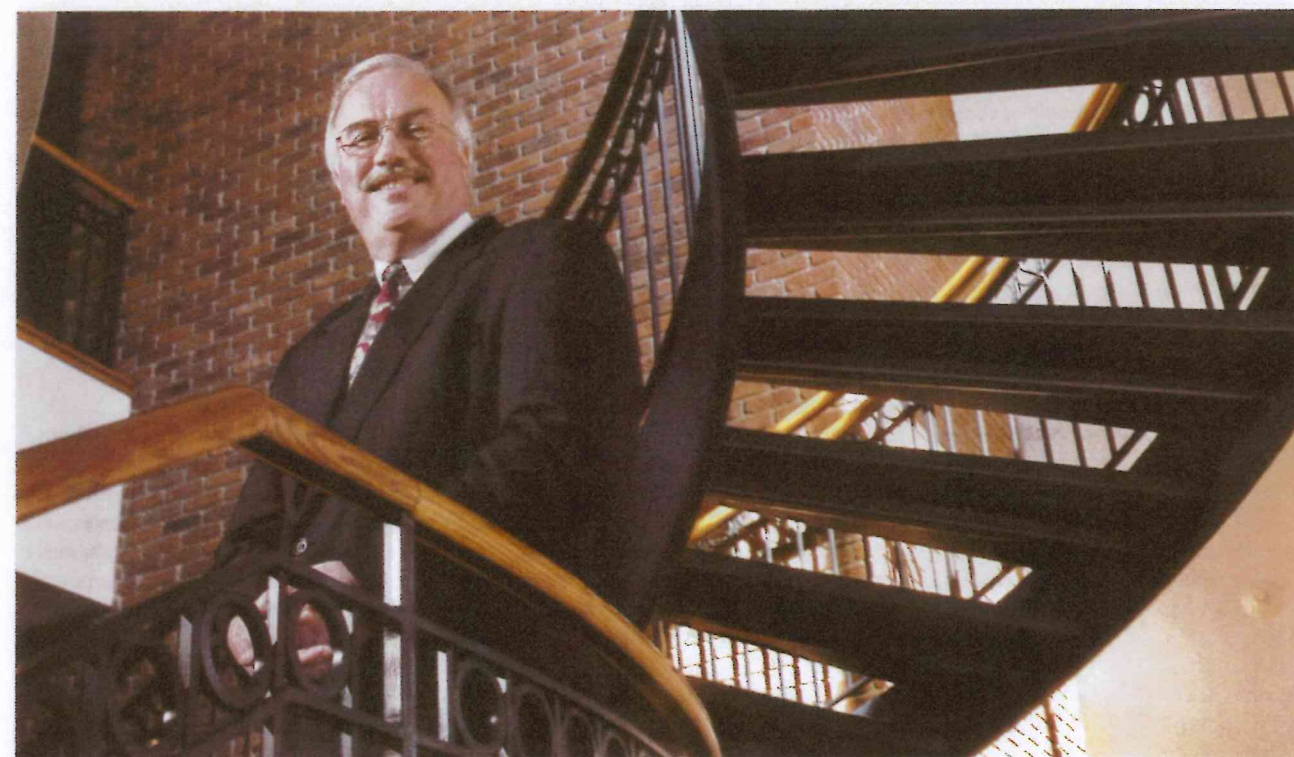


PHOTO BY JOHN BERRY

By ROBERT T. CHERRY, CPA, CVA; PARTNER, DERMODY, BURKE & BROWN, CPAs, LLC

It happens so often, it has become cliché: A family business owner holds the reins in a vise like grip, allows successors little say or control and refuses to step down when it is clearly time — causing the family, the business and the employees inordinate stress. For most family businesses, the transition of leadership is emotional and steeped in family politics. It is so difficult that just 33 percent of family businesses survive the transition from the first generation to the second, and only 16 percent survive to generation three. However, most transitional problems stem from one basic oversight: no formal transition plan.

A transition plan opens communications and establish-

es clear expectations grounded in fairness and shared values. Generally, retaining an outside, objective professional to help develop and execute a transition plan greatly increases the probability of success. A good transition plan helps prevent all three of the top transition problems:

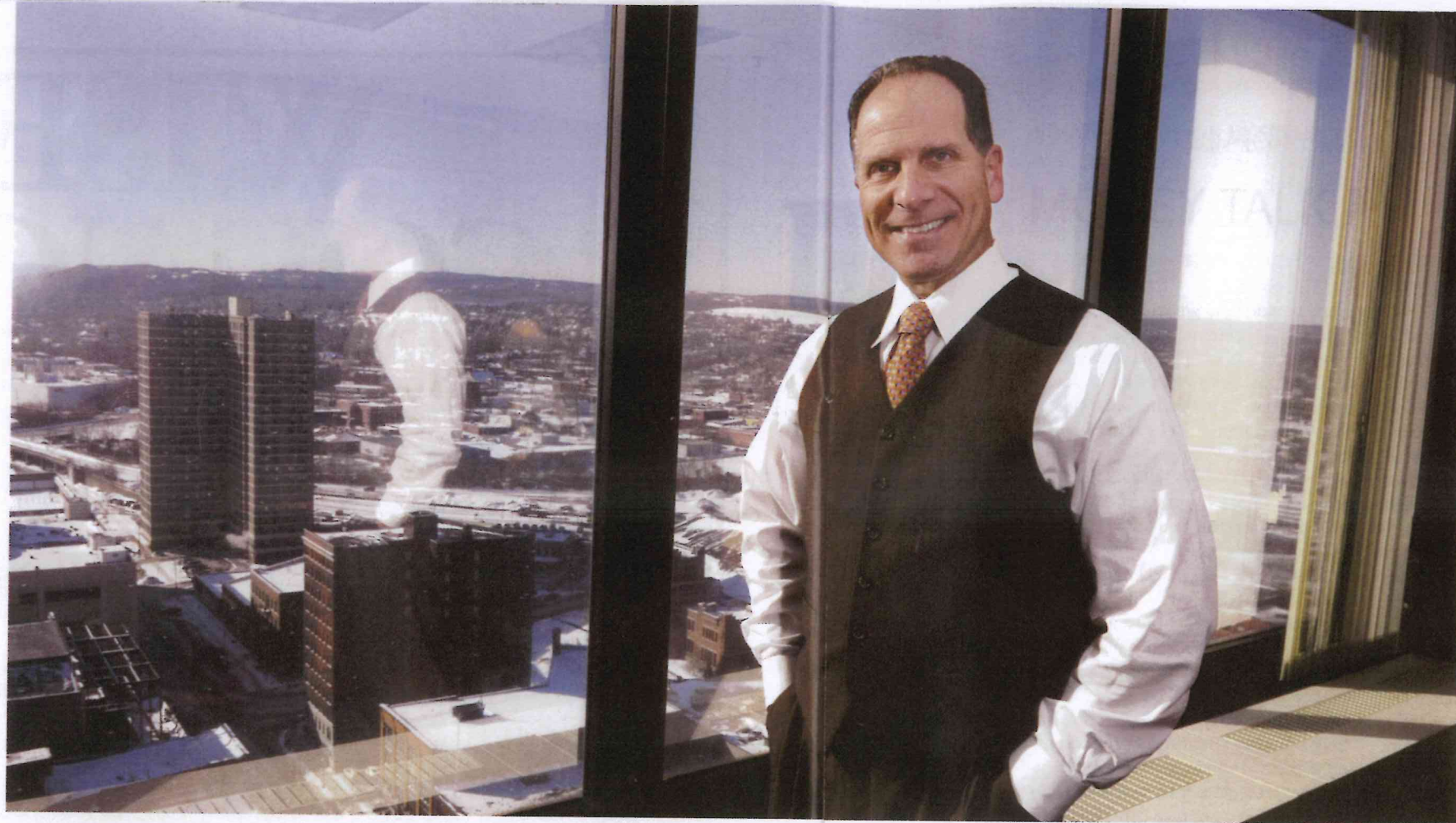
1. The first-generation leader will neither delegate nor step down.
2. The next-generation leaders are neither evaluated for skills and aptitudes, nor positioned properly within the company, nor formally developed as leaders.
3. Key non-family management team members depart when faced with an unknown future when the next

gen enters the business.

Common Plan Characteristics

- Transition plans often take effect when the next gen is quite young. As soon as family members show interest in the business, operational cross training begins, often starting with basic jobs, throughout high school and college.
- After graduation, some plans require the next gen to complete three- to five-year stints at large multinational companies to gain perspective and managerial experience. They also serve another important purpose: When the next gen re-enter the family business, it is positioned to gain credibility with non-family employees, who can otherwise become disgruntled and may leave.
- Most plans also call for the members of the next gen to undergo formal, objective assessments of their abilities, particularly to lead and grow the business. Not all family members will be CEO material, and identifying their strengths and where they can contribute — perhaps in sales, operations or HR — enables a company to educate and groom them accordingly.
- Key nonfamily management team members are provided with long-term financial incentives to remain with the company.
- Finally, perhaps the most compelling reason to employ a transition plan is to circumvent “tight-rein” syndrome. By the time a well-planned transition actually takes place, company leaders are well-prepared to hand the reins of the business to properly educated, thoroughly trained and experienced members of the family. Change is never easy ... but in a family business, developing a transition plan for the inevitable change-over in leadership helps effect an evolution, not a revolution, that ultimately benefits the family, the business and the employees. ■

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BY PHILIP I. FRANKEL, ESQ., BOND, SCHOENECK & KING, PLLC

Family businesses are unique entities with no definitive classification except being owned and operated by at least two related people. This can range from a husband and wife running a small bodega to a corporate conglomerate that is in the hands of a fourth generation of family members. Yet each entity faces similar legal and psychological concerns. In order to avoid a Griswold Thanksgiving, family businesses must establish a business plan, use a flexible corporate entity, draft agreements and treat the company as a true business, not an extension of the family.

It is common for family businesses to ignore the legal aspect of the company structure and “deal with it later.” This creates more problems later on when the family is dealing with succession planning, extended-family members and sharing in its success. Aside from the tax and liability issues, it is essential that the family select a flexible business model that allows it to take on the personality challenges of familial expectations, sense of entitlement, inheritance and worthiness, as well as spousal issues.

The family should set up a business entity with voting and nonvoting ownership to allow family members to share in the economic growth of the company but not necessarily the management. More importantly, the family needs to draft a shareholders agreement to codify the business strategy and intent. For example, most families want the stock ownership to remain with their heirs. Thus, they must address the restrictions of stock ownership. Can a spouse own the shares or will it be limited to direct descendants of grandfather? How do shares get sold and how are they calculated? What if a son or daughter wants to sell his or her shares? What happens in the event of the death or permanent disability of a family member? Since family businesses want privacy, they very well may require private arbitration to resolve disputes rather than have their dirty laundry aired publicly in court. All of these issues and more are incorporated into a shareholders agreement. These issues must also be coordinated with each family member's estate planning to make sure their mutual intentions are carried out.

PHOTO BY DAVID LASSMAN

Since new generations bring more people, ideas and problems, the company must continuously review its business strategies and its business documents. It must have a flexible plan that will accommodate both the family's long-term goals and the business interests. ■

Philip Frankel has been devoted to business and corporate transactions with emphases on startup companies, handling employment matters, contractual negotiations and intellectual property concerns. He frequently lectures to companies, trade associations and attorneys on issues involving employment law and intellectual property development and protection.

PHOTO BY DAVID LASSMAN



BY MARK WASMUND, MACKENZIE HUGHES

Succession planning for a family business involves the often inherent conflict between “family” and “business” interests. This conflict often intensifies when the business constitutes the major asset of the principal's estate. The primary issues in succession planning can be categorized into three main areas: business operations, family considerations and financial interests relating to both family and business.

The issue of business continuity is one of pure practicality. Careful consideration must be given to identifying the person best suited to running the business once the principal has departed. An objective evaluation must be undertaken to determine whether the next generation of the family has the expertise, management skills and interest to take command of the business. If more than one member of the family is involved in the business, a critical analysis must be done regarding the relationship between those family members and other key employees within the business.

The key to dealing with the practical considerations of business continuity are ensuring communication and advance planning through management, employment and/or shareholder's agreements. This will ensure that each person knows their particular role and understands the principal's intended plan regarding the continuity of the business. These agreements can also be utilized to establish salaries and benefits to avoid later disputes.

Family considerations involve providing for all family members within the principal's estate plan while incorporating the business into a fair estate plan. A crucial element is evaluating the business. If the business constitutes a large percentage of the estate, a determination must be made as to whether, and how, ownership and control of that business will transfer to the principal's intended beneficiaries. If the plan includes the business passing to all beneficiaries, the inherent conflict between those managing the business and those outside the business must be addressed. Valuation can be a contentious issue. To avoid valuation disputes in an estate, sales to the family members in the business during the principal's lifetime should be considered. This may alleviate concerns of those involved in the business regarding their monetary control. It will also establish the value of the business for incorporation into the overall estate plan.

It is essential that the financial composition of the business, as well as the entire estate, be determined. If it is likely that the estate will have liquidity issues and the plan is structured to leave the estate in equal shares, a beneficiary not involved in the business could be at a disadvantage. Alternatively, it could force a beneficiary involved in the business to borrow against the business to buy out the outsider's share.

One possible solution is life insurance. Structured correctly, life insurance proceeds can provide the necessary flexibility and liquidity. A planned buyout during the lifetime of the principal can also reduce pressure on the estate and provide for needed cash flow. Thorough planning, communication and objective evaluation well in advance of the principal's departure from the business are the keys to any successful succession plan. ■

Mark W. Wasmund joined Mackenzie Hughes in 2010 as a partner in the business department. He focuses on all aspects of real estate transactions, representing buyers, sellers and lending institutions in both commercial and residential transactions.