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Constructing a Succession Plan

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Biosketch




- ✓ Originally from Southern Minnesota
- ✓ Lives in West Des Moines, IA with his wife, has three adult children and nine grandchildren
- ✓ CERTIFIED FINANCIAL PLANNER™ (CFP®) practitioner
- ✓ Accredited Estate Planner
- ✓ Masters of Science in Financial Services
- ✓ 40 years experience in financial services and planning
- ✓ Is one 60 Heritage Design Professional (HDP) in the United States



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Agenda

- ✓ Taking inventory of your current personal and business situation
- ✓ Critical conversations with key stakeholders
- ✓ Identifying issues where action is needed and formulating alternative scenarios for execution



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Three Stages of Family Business

from John Ward's Perpetuating the Family Business

- ✓ Stage I – Owner-Managed
- ✓ Stage II – Sibling Partnership
- ✓ Stage III – Cousin Collaboration
- ✓ Cold hard facts
 - 30 years ago – 5-10% run by siblings
 - Now: 50% owned/run by brother/sister groups
 - ½ family businesses fail to go to 2nd generation




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#1 Conclusion after 40 Years of Working with Business Owners

- ✓ Decision is NEVER made until it's put on paper.
- ✓ **Complete this sentence:** "If I go back to the farm/ranch, my expectations are..."
 - what potential successors are thinking...
 - what owners are thinking...


"...the shortest pencil is longer than the longest memory!"
Mark Patterson, *The Circle Maker*



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Table Exercise: Succession Planning Self-Assessment

- ✓ Page 27 – Legacy Project Workbook
- ✓ Answer questions with 1-5 score
- ✓ Don't worry about totaling your score – not all questions are a "score able" with a number
- ✓ Team scoring is acceptable...or NOT!
- ✓ Add: *The right to work in the business should be earned...it's not a birthright.*



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Step # 1 – Transition Planning

- ✓ Take inventory of current business operation
 - Management
 - Ownership
- ✓ Put it on paper!
 - For owners
 - For potential successors
 - For advisory team *"why these guys?"*
- ✓ Define where you want to go in the future



Basic Succession Planning Questions

- ✓ What is our mission, vision and value set?
- ✓ Needs of the business for capital (now & future)?
- ✓ Needs of the business for management and staff (now and future)?
- ✓ Capacity to support current and future families desiring ranch career (financial trends, margins, revenue/FTE)?



Transitioning Wealth (Ownership & Financial Control)

- ✓ Optimal entity structures to facilitate goals?
- ✓ Buyout agreements, gifting, wills, estate plans, etc.?
- ✓ Risk management (insurance) tools needed to insure liquidity and facilitate transfers?

Warning! Answer these last... not first!
"...form follows function"



What are you passing on?

- ✓ Ownership
- ✓ Working Career Opportunity
- ✓ Values

Mission and Core Value Statements

- ✓ Only 33% of ag businesses define this!
- ✓ Consequences: Team can't agree/focus on:
 - Mission – business product or service, primary customer & key objective
 - Vision – end point if you succeed
 - Values & Philosophy – ground rules
- ✓ Put in writing and post visibly on farm



Our Vision

Our Mission Will Be Accomplished When...

- ✓ Complete careers with financial security and value our family and business associations
 - ✓ The business grows, adapts, and remains financially viable
 - ✓ Capable successors are carrying on our heritage
- What's your exit plan?** ← Not everybody's goal

Common Conflicts – Core Values

- ✓ Always be leading edge...
 - "If ain't broke, don't fix it"
- ✓ Maximize profits (live for today)
 - Maximize long-term economic and environmental sustainability (live for tomorrow)
- ✓ God & family first
 - Business first; God and family can wait
- ✓ Professionalism always expected
 - Professionalism OK when I'm "in the mood"
- ✓ Everybody should be equal
 - Pay and position should be based on skills and performance



Consequences of "Bad Chemistry" & Lack of Consensus Vision & Core Values

- ✓ Manage for "today" vs. "Long run"
- ✓ Make rules on the go
- ✓ End Result:
 - At each other's throats!
 - Chase successors away
 - Sever business & family relationships
 - Run business aground

Planning References – Legacy Workbook

- ✓ See pages 32–36 Building Business Plans
- ✓ Need to sort out PLANNING as a part of the Business Management Process from term "Business Plans"



Why Farmers Don't Have Time To FARM!!!

- ✓ Production Planning
- ✓ Marketing Planning–73%
- ✓ Financial Planning
- ✓ Contingency Planning
- ✓ Strategic Planning -19%
- ✓ Manpower Planning
- ✓ Succession Planning
- ✓ Retirement Planning
- ✓ Family Planning

"Simplify" Planning and Understand "Inter-Relationships"

- ✓ Operational or annual planning
 - Production Plan
 - Marketing Plan
 - Capital purchases and sales
 - Debt financing arrangements
- ✓ Strategic or long range planning



Goals and Action Plans – Succession Planning *What are you reaching for?*

- ✓ Goals **28% do this**
 - Get them on paper – don't need to be fancy
 - Personal & Business
 - Identifies stakeholders intentions & wishes
 - Dispers myths and erroneous assumptions
- ✓ Action plans
 - What, When, Who
 - Budgets, Cashflows
 - Resources required
 - Feasibility

Are these Strategic Issues Defined and Assessed Periodically?

- ✓ Growth
- ✓ Business structuring
- ✓ Estate & retirement planning
- ✓ Transfer of ownership/management
- ✓ Capital improvements/replacements
- ✓ New enterprises or enterprise shifts
- ✓ Manpower Planning / Personnel Development
- ✓ Management System Refinements
- ✓ Strategic Alliances & Joint Ventures
- ✓ Environmental Stewardship
- ✓ Tillage strategies – Conventional, No till



Consequences...

Lack of Professional Planning Approach

- ✓ Unexpected outcomes
- ✓ Outdated strategies – can't compete or exploit opportunities
- ✓ Don't optimize decisions – purchase vs. rent vs. hire/share
- ✓ Anxiety & Stress destroy business teamwork & extended family ...
 - **ESPECIALLY TRUE IN SUCCESSION!**

Who should be on bus, and where do they sit? Good to Great by Jim Collins

- ✓ How are you organized today?
- ✓ What will organization look after transition?
- ✓ Criteria be for filling "vacant slots"?
 - Skills, abilities, passion vs. "I'm family; I'm owed a job"
- ✓ How do you pass the baton? (see pg. 42)
 - Duty statements review, timetables for transition, apprenticeships, OJ training
- ✓ How does old guard get out of the way?
 - Board chairman vs. CEO ("boss")



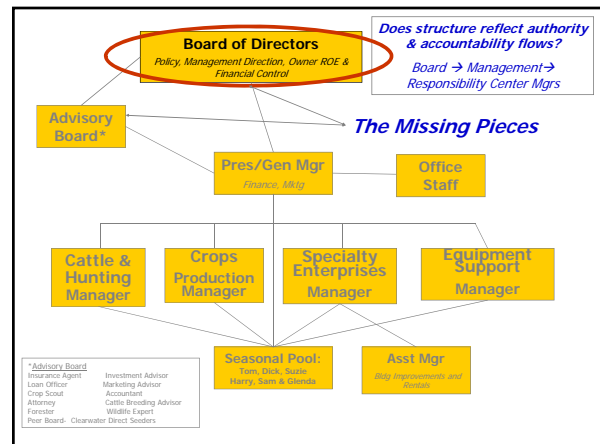
Organization Questions

- ✓ Are roles divided?
- ✓ Is reporting and accountability structure defined?
 - Now
 - After transition
- ✓ Do key members have written job descriptions?

40% have this in place

Table Exercise: Organization Structure & Players

- ✓ Turn to Page 37 to draw picture
- ✓ Relates to Question #3 on page 35
 - Draw flowchart of members "active" in operation
 - List title or area of responsibility for each
 - Include board members/advisors, if applicable
- ✓ Extra Credit: Draw chart 5-10 years from now





Is career path apparent?

CEO

Assistant Manager


Grunt

Board Chairman





Why Write Job Descriptions?

- ✓ Pinpoints accountability for team members
- ✓ New “hires” – focus on skills and qualifications
“I’m family...I’m owed a spot here.”
vs. *Do we have a vacancy to fill?*
- ✓ Basis for performance appraisal
- ✓ Retirement transition tool
 - Helps exiting principal focus on key decision areas
 - Checklist for training and delegation strategy
 - 56 DUTIES listed in Guidebook




Role of Board of Directors

- ✓ Setting Policies
- ✓ Determining strategic direction
- ✓ Hiring, directing, evaluation & compensating management
- ✓ Maintaining financial control
 - reviewing performance
 - exercising “due diligence”




Job Description – Chairman of Board

- ✓ Policy review and refinement
- ✓ Investment analysis
- ✓ Strategic planning
- ✓ Hiring, coaching, grooming successors
- ✓ Performance review and feedback
- ✓ “Assisting” and “advising” successors in day-to-day operations without telling them what to do



Challenge: Mentoring vs Micro-managing

- ✓ Making the transition from...
 - Boss/CEO to Board Chairman
- ✓ “Graduating”
 - From Parent
 - To supervisor, manager, mentor, delegator, enabler, groomer
 - Tools: tone of voice, words, body language



Advisors Can Play Useful Roles

- ✓ Defining **board roles**
- ✓ Setting **compensation** – board, CEO, “Blood family”
- ✓ **Strategic planning**
- ✓ **Ownership transfers** (capital injections/withdrawals)
- ✓ Getting **incompatible players** “off the bus”
- ✓ **Champion** for “disenfranchised” owners
- ✓ **Guiding financial analysis** discussions
- ✓ **Running effective meetings**—board, family council
- ✓ **Transitioning management** duties
- ✓ Sounding board for **family conflict** issues



Selecting the Successor

- ✓ Does process differ if DAD:
 - is involved in the picture?
 - not around to influence the process?

- ✓ Does it make a difference:
 - who is older?
 - who has more tenure?
 - whether candidate is male or female?
 - who has the most ownership?



POSITION: President/General Manager

Administrative Responsibilities

- Coordinate operational & strategic planning
- Organize work force
- Staff (recruit, hire, train) and assign responsibilities (job descriptions)
- Coordinate workflow
- Administer communication, evaluation and control systems
- Execute contracts
- Provide information and policy input to board of directors



Farm Management role usually combines with technical role.

Avoid "Bossing Tendency" Define Attributes of Ideal Manager



Rain break weaning calves

- ✓ Facilitator...not boss
- ✓ Empowers people...doesn't micro-manage workload
- ✓ Focuses on people, resources, information, technology
- ✓ Promotes teamwork, positive thinking and professionalism
- ✓ Willing to be accountable to the "board of directors"

Policies & Practices

- ✓ Do policies and SOPs attract & retain successors?

- ... or

- ✓ Chase them away?



Are Policies Written Down? 36% do! ...Common "Land Mines"

- | | |
|-------------------------------------|-----------------------------------|
| ✓ Housing | ✓ Family Employment Policy |
| ✓ Company vehicles | ✓ Medical benefits |
| ✓ Room and board | ✓ Retirement plans/pensions |
| ✓ Expense accounts | ✓ Business benefit continuation |
| ✓ Setting compensation | ✓ Workdays and holidays |
| ✓ Withdrawals of capital | ✓ Vacations, sick, business leave |
| ✓ Insider/inter-entity transactions | ✓ Buyout Understandings |
| | ✓ Outside activities |

Ask each member of team to write down understandings...then compare notes!



Housing, Utilities and Meals



- ✓ Housing provided by business or individual?
- ✓ Who pays for: maintenance, insurance, electricity and phone service?
- ✓ Meals on work premises

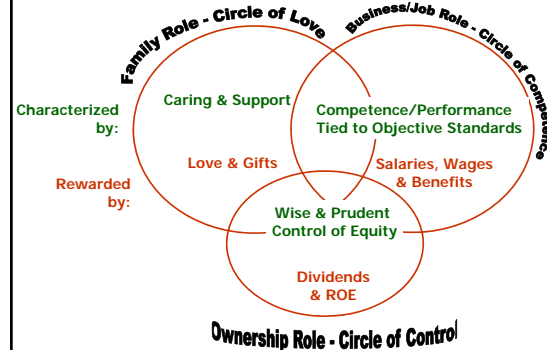
Salaries, Wages & Bonuses

- ✓ Officers / Partners
 - Monthly draws
 - Annual salaries, bonuses

- ✓ Full & Part-time help
 - Who determines pay scale?
 - What is the pay cycle?
 - When is a bonus appropriate?



3 Circles of Compensation



Common Sins - Compensation

- ✓ inequity between off farm kids & "insiders"
- ✓ bosses kids get preferential treatment
- ✓ using labor as source of operating credit
- ➔ ✓ confusing compensation with estate planning
- ✓ no differentiation in pay scale
- ➔ ✓ inconsistent allocation of earnings to Labor/Mgmt vs. Owners



Family Employment Policy

Components to keep professionalism in the family business

- Vacancy requirement & skills required before hiring
- Economic capacity analysis to support hire
- Prior experience/training required; apprenticeships
- Supervision and reporting relationships/nepotism rules
- Consultation of stakeholders required before hire
- Merit vs. paternalism as criteria for hiring and advancement
- Policies on pre-nuptials
- Discriminatory treatment - family vs. non-family stakeholders
- Correlating compensation/bonuses with responsibility and performance



"...Policy before the need"

Danger Zone: Abusing "Family Preference"

- ✓ **Nepotism** has bad connotation for a reason!
 - Preferential compensation: "...pay mine more because..."
 - "right name" gives special rights (12 yr old at potato dump year; spouse driving truck @ harvest)
 - *Unemployed kid...*needs job. "Let's find a place for him."
- ✓ Relevance to Transition Planning
 - Assess commitment to running it like a business
 - "All in...or all out"– rules must apply to ALL
- ✓ Solution: Address in *Vision/Value Statements* and *Family Employment Policy*



Capital Contributions, Withdrawals

... 22% have policy in place.

- ✓ Who is welcome to invest in farm/ranch?
- ✓ Should everyone be "equal?"
- ✓ Minimum capital to leave invested? "*Can I ever get my money out?*"
- ✓ Revenue sharing tied to ownership ratios?
- ✓ Compensation for excess balances?
- ✓ Whose monitoring capital balance compliance with legal agreements?



SOP's, GAP's

30% have these




- ✓ *Not something new!*
- ✓ Purpose: guidance documents for repetitious or routine jobs
 - Training tool – new hires
 - Assures jobs are done following BMPs, GAPs
 - Increases safety & lowers cost of production
 - Baseline for measuring job performance, auditing
 - *Great job for mentor, coach phasing into retirement!*



Communications Systems

...Do you:

- ✓ Agree on rules for communicating professionally?
- ✓ Invest in understanding personality styles? **Poll Group**
- ✓ Share records openly? **40%**
- ✓ Hold Regular Meetings – Staff, Mgmt, Owners, Family? **42%**
- ✓ Documentation key understandings? **31%**

"Meeting culture" in your business?

- ✓ Staff meetings
- ✓ Management meetings
- ✓ Owner board meetings
- ✓ Advisory board meetings
- ✓ Family meetings ←
- ✓ Family council meetings



Communication challenges - Family Farm Businesses

- ✓ Don't think business rules apply
- ✓ Family status trumps business roles
- ✓ Expected "unprofessional" to be tolerated
- ✓ Don't consider impact of personality style differences




Key Elements:

Management Control System

- ✓ Comprehensive Record Systems
- ✓ Regular Performance Reviews – Individual & Farm Business
- ✓ Ongoing Training & Professional Development
- ✓ Use of Outside Advisers
- ✓ Good audit and internal control systems




What gauges do we monitor?



- Seeding Rate
- Temperature
- Oil Pressure
- Acres/Hour
- Gallons/Acre

- Working Capital
- Debt/Asset Ratios
- ROE & ROA
- Accrual Net Income
- Cap Debt Rep Capacity
- Unit Cost of Production



Sharing Financials with Successors

- ✓ Have you done this?
 - If yes, how do it go?
 - If no, what are your fears?
- ✓ Successful attempts...
 - Ag lender, facilitator, family business advisor, acct.



Sharing History with Successors

- ✓ Do you have this written?
 - Key events and timelines that shaped your business journey
 - Ownership evolution
 - Key players that have come and gone
 - "skeletons"
- ✓ Value in succession planning process
 - Defining your "legacy"
 - Briefing document for outsiders



Are Key Principals Evaluated?

Only 20% do evaluations

- ✓ Develop innovative system that fits your business
- ✓ Set performance standards tied to job description
- ✓ Use disciplined process on regular basis
 - Anybody exempt? (boss, family?)
- ✓ Balance praise & criticism



How Do We Avoid Tragedies?

...put it in writing!

- ✓ Define vision, values & management process for those moving forward
- ✓ Put right people with right talents in right seats
- ✓ Separate the "train tracks" – ownership vs. labor/management
- ✓ Reduce retirement fear – extend career path for patriarchs & groom successors
- ✓ Set goals & develop strategy to reach targets
- ✓ Implement professionally; engage advisory team & peer networks
- ✓ Commit to accountability – review performance *regularly & honestly*



The Farm = Children's "First Business School"

- ✓ Children learn first lessons of business
- ✓ We can teach:
 - Good business principles, or
 - Bad habits
- ✓ Lessons taught = heritage we pass on



Where to Start? ...Concerned Parent

- ✓ **Appoint "on-site" Transition Coordinator, or Transition Task Force**
- ✓ Map out "transition steps" and "management process" needing clarity
- ✓ 3 D's – Discuss, decide, and document
- ✓ Organize information – (3-Ring Binder)
- ✓ Join peer networks; form advisory teams
- ✓ Attend management training
 - TEPAP, Harvard AgBus Seminar, Top Prod.

Who can help?

- ✓ Tap “qualified/certified” facilitators and resources
 - Family Firm Institute
 - Farm Journal Legacy Project
 - Purposeful Planning Institute
 - FamilyBusiness.Ag
- Make study of Family Business excellence a lifelong journey



Where are we in agenda?

- ✓ What we just did:
 - Took inventory of crucial conversations, issues, and options to consider about business we hope to pass on
- ✓ Next up:
 - Legal issues discussion
 - Tax and Estate Planning issues discussion
 - Execution and Implementation – Actionable Steps
 - Wrap Q & A

