Summer 2016 • Volume 13 / Issue 2

Gene Siciliano

Succession and exit strategies are NOT the same

I recently read an article by a professional advisor – OK, a competitor – who said in his article that an exit plan can also be referred to as a succession plan. Sorry, but that's just not true. They're different strategies intended to accomplish very different objectives, and the actions that a business owner will take to implement a succession plan will be different from those intended to achieve an exit at the highest possible price.

Let me explain. First, a more accurate definition of each term:

"...that's just not true."

A **succession plan** is one in which the owner wants to turn over the running of the company to either family members or members of the internal management team. This may or may not involve a change in ownership in the company. An employee stock ownership plan (ESOP) is an example of a succession plan that also involves a partial or complete transfer of ownership. But often a transfer of operating control – such as to the children of the owner – will involve retaining some or total ownership and primarily relieving the owner of the daily duties of running the company. In any event, the involvement of the owner doesn't suddenly stop.

An **exit plan**, by contrast, is just that – a planned exit from all responsibilities of running the company AND a divestiture of the owner's ownership interest as well. While it's true that some exits involve the owner remaining partially involved for some period of time, this is usually a condition of the sale designed to maximize the purchase price or ensure that any contingent elements of the purchase price are resolved in favor of the seller.

It's true that both plans have some key elements in common, such as a formal valuation of the company, extensive tax planning, lots of legal papers to prepare, review and sign, and a lead time sufficient to implement the changes that are needed in the business. What differentiates the strategies is not their similarity but their differences. For example, a succession involves passing the company to people who already have knowledge of it, while an exit involves a sale to outsiders, possibly not even familiar with your industry. So, let's clarify briefly how those preparation steps are likely to differ.

Some of the unique elements of a succession plan that would not typically apply to an exit plan:

- Identification of the person or persons who will run the company in the future, perhaps in the form of a pro forma organization chart
- Where children are the preferred choices, an objective assessment of their willingness and ability to assume the roles to be filled, with or without parental involvement
- Where the management team will be the successors, an objective assessment of the new leaders' preparedness for taking on that role
- A plan for providing training/coaching to fill important gaps in knowledge or experience
- Identification of functions that must be filled by new addition(s) to the team because the designated successors don't have the ability/affinity/time/experience to fulfill them

Some of the unique elements of an exit plan, by contrast:

- Definition of discrete actions that should be taken to increase the Enterprise Value (EV) of the company, and then the "sub-plan" to implement as many of them as possible
- Consider whether an audit by outside CPAs will be needed to support the numbers, especially if the company has never had an audit before

(continued on next page)

Gene Siciliano is the founder and president of Western Management Associates, source of *Your CFO for Rent®* services for over 25 years. The firm provides interim and part-time CFO/Controller services, executive coaching and assistance in operational finance and exit strategy. Gene and his team of seasoned CFOs and controllers have a clear mission in their work with CEOs and owner/operators of privately owned companies. Their value proposition:

- Increase the company's net worth and profitability by improving the management team's financial proficiency and bottom line results, and
- Develop and execute strategies that will make your company more appealing to a buyer or investor, if and when the time comes for an ownership transition.

Succession/Exit

(continued from previous page)

- A dry run financial due diligence review to help prepare for the real one when the first prospective buyer's Letter of Intent (LOI) shows up, along with their CPAs
- Because more must be done to raise EV in the mind of an outside buyer, start 2 to 5 years before the desired exit date – there is much to be done in the best of companies
- Engagement of an investment banker (or business broker for small businesses) to identify/contact/engage prospective buyers and create a competition among them for the highest possible price

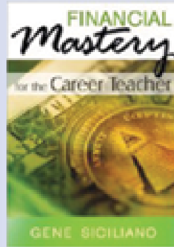
> *"If you don't understand the details of your business you are going to fail."*
> —JEFF BEZOS

Admittedly this is a short and incomplete list of differences, but I hope you get the point. While a decision to move forward with a succession will involve much less complex planning than a sale and exit, neither is a walk in the park. Recognize which direction you want to go, pull together your team to lay out the plan in detail, and don't confuse succession with outright exit.

In either event you will need strong internal expertise in key areas to pull it all together, to drive EV improvements, and to measure the progress along the way. We've found that the weakest area in most companies is the financial function, which is why I launched my firm 30 years ago. We will put a seasoned, financial executive into your company for as long as needed to ensure the deal gets done as smoothly as possible.

Your CFO for Rent, **for a few weeks, a few months or a few years**. Call us. We can help you keep your plan on track.

SUPPORTING GROWING COMPANIES SINCE 1986



Gene Siciliano
WESTERN MANAGEMENT ASSOCIATES

P | 888 788 6534
O | 310 645 1091
E | info@CFOforRent.com

www.CFOForRent.com