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than
money

Succession planning:

A how-to guide for business owners

The topics covered

Getting started

There's a fundamental misconception about succession planning – that it's done at the end of a business owner's journey.

In reality, succession is simply another stage of a business' life cycle; planning for it should begin long before it's put into action.

"People associate succession planning with retirement," says Rex Afrasiabi, founder of specialist law firm New Chapter Legal. "In my opinion, it's not about retirement, it's about growth."

All the more reason to start planning early. As NAB Professional Services Executive VIC Adam Holster says, "While the details will often become more concrete as the transition draws nearer, the groundwork can definitely be laid earlier."

01

Where to begin

Firstly, you need to examine your business goals, Holster says. “Is it growth? Is it attracting or retaining amazing talent? Succession is a mechanism to make that happen.”

Then consider the best strategy to achieve those goals. That might involve one or more owners exiting the business, but a strong succession plan can be so much more.

A well-executed succession plan is an opportunity to evolve a business into a more mature, more secure entity. It can strengthen the business by reconfiguring ownership, operating practices and financial structure, among other things.

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Key takeaways

- A succession plan is an opportunity to strengthen your business
- Start your plan by understanding your business goals
- Build a strategy around those goals

02

Consider what’s right for you and your business

There’s no perfect approach to succession. One of the primary questions, however, is whether you want to exit the business completely, or simply dilute your ownership.

While it might be tempting to sell up and realise your gains, reducing your shares in the business also has advantages. It could be an opportunity to stay on in a part-time or advisory role as you transition to retirement. That way, you benefit at a personal and financial level while the company still benefits from your experience.

Whatever your plan, it’s important that it be robust. “It [should] celebrate what makes your business unique,” Afrasiabi says. “[That way it can build on] your and your business’ success, rather than try[ing] to fit it into a situation or contract that doesn’t suit you or your stakeholders.”

Key takeaways

- Choose an option that builds on your business’ success
- Selling is an opportunity to realise your gains
- Diluting your ownership can benefit you personally and financially

03

Don't forget your people

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When identifying the key positions, look not only at the sales directors – look at the general manager, the office manager, the head of property management.”

Rex Afrasiabi
New Chapter Legal

Key takeaways

- Look beyond your sales directors when identifying key positions
- Ensure key staff and incoming shareholders are ready to take over well in advance
- Involve key talent in your ongoing succession plan discussions

A well-considered succession plan ensures the right people are on board.

“When identifying the key positions, look not only at the sales directors – look at the general manager, the office manager, the head of property management,” Afrasiabi says.

You also want to ensure they're ready for any new responsibilities well in advance – as are any incoming shareholders. If they're to manage the agency's daily operations, for example, they may need 3-5 years' training and experience before taking over. Business owners often leave this too late, Afrasiabi says.

The good news is that many owner-operators are already incorporating some succession planning into their human resource management.

You may be cross-training key staff in aspects of the business outside their core competencies, or discussing how careers will evolve. If so, you're laying the groundwork for continuity beyond a succession plan.

Better still, when key talent is involved in those discussions, part of your succession plan becomes theirs as well. “They know what their future holds and where you're taking them,” Afrasiabi says.

04

What documents do I need?

Regulations around transferring a business are always evolving, so it's important to seek legal advice – preferably from a specialist firm. Also helpful is your own basic understanding of legal requirements and liabilities.

Important legal documents you might rely on include:

A non-disclosure agreement: Non-negotiable before you start any discussions.

A contract: Depending on whether a business is being sold or diluted, the contract will be either a subscription agreement or a sale of shares or units agreement.

A partnership agreement: A bespoke, well-considered partnership agreement (called a shareholders agreement or unitholders agreement) will help the business continue to run smoothly. "Disputes don't spring from bad intentions – they come from misunderstandings," Afrasiabi says. "Make sure your partnership agreement is specific to what a agency does."

To further protect yourself, you should also consider:

Warranties: If anything comes up before the purchase date, the vendor should be responsible. "From a vendor's perspective, you should be offering that," Afrasiabi says. "[However,] you can also reduce and limit your exposure by writing that into the contract."

Restraint of trade conditions: Depending on the deal, the parties may want to consider restraint of trade conditions for key staff involved in any succession transition.

Key takeaways

- A robust partnership agreement will avoid misunderstandings
- A non-disclosure agreement is a must before you enter discussions
- Seek legal advice from a specialist if possible

05

Get all your ducks in a row

Key takeaways

- Make sure your house is in order before your business is valued
- Financiers will potentially lend up to 70% of the valuation figure
- Ensure your team has sufficient experience valuing similar businesses

Before exiting all or part of your business, you'll want to ensure your house is in order, including paying outstanding taxes and complying with any ASIC requirements.

As Holster says, "It's a lot of the boring stuff but you want to be sure it's all there. If not, settlement may be delayed."

It will also help with valuing your business and, therefore, obtaining any finance you might need. "Financiers will want to look at the valuation of the business itself, and potentially lend up to 70% of that figure," Holster says.

Other factors to consider include:

- **The sales business component:** This is more complex than rent roll, but if a business has more sales agents it will become more relevant. "Any agents not exiting the business contribute to the valuation at a 10-25% multiplier of the revenue they generate," Holster says.
- **Plant and equipment**
- **Intellectual property**
- **Cash held**
- **Loans**
- **Tax liabilities**
- **Employee liabilities**

Again, the quality and experience of advisory capability is crucial. "Make sure you're really comfortable that your bookkeeper or accountant has seen at least 10-20 examples of similar valuations," Holster says. "Questions about valuation shouldn't baffle your advisory team."

In conclusion...

Succession planning is an important part of any long-term business plan – not just a last-minute pathway to retirement. With the right strategy, execution and advisory team, a good transition can make a business stronger.

For more information, speak to your NAB business banker today or visit nab.com.au/securingthefuture