The Question No One Asks: Could Your Business Survive Your Death?

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The Uptake: While it's difficult to imagine your business running without you, the inevitable will happen. Learn how your business can survive after you're gone.

The satisfaction of building a business from the ground up is undeniable. That satisfaction grows if your children — or other family members, for that matter — join in your efforts. Owning a family-run business gives you the distinct honor of passing along not only years of invaluable knowledge and experience, but also a career and lifestyle to the next generation.

Unfortunately, creating and preserving that legacy is never easy. I learned this lesson the hard way when a series of unanticipated issues led to a rocky transition for our family business following my father's death. We had a buy-sell agreement in place, but it wasn't properly funded with adequate life insurance — we eventually ended up selling the company to a national competitor and suffering family turmoil.

Navigating Tough Transitions

After researching the issue further, I realized that our family wasn't alone. In fact, only 30 percent of family-owned businesses are successfully passed to the second generation, and just 10 percent transition to the third.

How do these inheritances fall apart? Reasons vary from family conflict to unprepared leadership or disparate visions, but the number one cause is that many owners of family-run businesses fail to take the time needed to develop a comprehensive succession plan.

Here's what must be done to help ensure your business remains successful after you're gone:

1. Agree upon who will take over the business. Discuss which key person or persons would be best suited to take over the company. This not only relieves some of the unavoidable burden that will be brought on by your passing, but also outlines terms of the change in leadership, such as appointing the next CEO, or presenting the option to buy out the surviving spouse.

We ran into this problem when my father died and each brother received a third of his company. That seemed fair on the surface, but without one clear leader to oversee the business, we were forced to awkwardly lead by committee. Choose a single individual to take majority control — while this may be a tricky decision, it will help to ensure a seamless transition. Be careful to choose the leader based on an honest assessment of leadership skills, commitment and business/financial acumen, NOT on birth order or family assumptions.

2. Institute sound accounting controls. Make sure all accounting controls are easily verifiable, with multiple people handling financial transactions. A system of checks and balances can deter others —

including trusted confidants — from giving into temptation and embezzling from the company down the road.

3. Formalize plans upfront – years before you believe they'll be needed. To guarantee ownership transfers to the correct person, have a formal buy-sell agreement in place to clarify the terms of the transition and reduce the risk of future infighting and litigation.
Aside from the standard contract, you might also consider a unilateral buy-sell agreement. This establishes a contingency for the company to stay in business without your family having to worry about dispositions once you're gone.

4. Arrange for funding of the transfer. Few people are aware of the funding aspects of buy-sell agreements. You can't just specify who will take over after your death or retirement— these acquisitions are considered purchases, not gifts. There are many methods for funding a buy-sell agreement; using life insurance is one method of handling the transaction. The agreement should address how the value of the company will be determined and cite a policy to fund the transfer. If the policy ends up being insufficient, then a promissory note should be issued to pay off the remaining amount over a period of time.

This as another obstacle that my family encountered when we found that there wasn't enough life insurance to purchase all of the stock from our mother. We had to start funding a pension plan for her by taking money out of the company's operating budget. If our parents had made sure the agreement was properly funded, the process would have been much smoother.

5. Build a collaborative team. These agreements are complex - work with a financial adviser, an accountant, and an attorney to draft a buy-sell agreement that covers all contingencies. Consider working with a collaborative advisory team to make sure nothing is overlooked.

Planning your succession strategy early, thoroughly exploring all aspects of the transition, and documenting the plans is your best option to safeguard your legacy for your family.

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