

Ownership vs Operational Succession

By Graham McBride



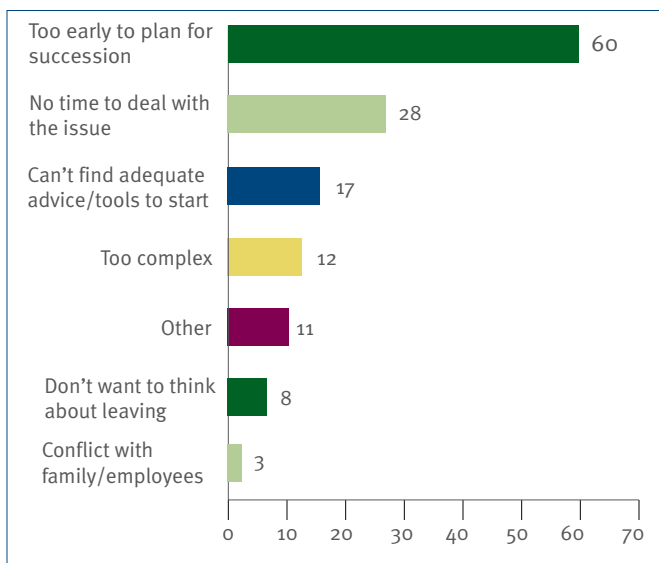
You can realize some of your equity and still retain control of your business

A lot of Canadian business owners assume that the day they give up the ownership of their business is the day that they relinquish all operational control. Many view succession as a one-off exit event that can be dealt with when the time arrives. It's one of the reasons that Canadian business owners are often greatly unprepared for succession. The reality is that the succession process doesn't have to be that rigid and it is never too early to start the ball rolling.

figure 1.

Why SMEs Do Not Have Succession Plans

(% respondents)



source: CFIB

Although 41% of all Canadian small and medium enterprise (“SME”) owners intend to leave within the next five years, less than half have any form of succession plan in place, according to a report from the Canadian Federation of Independent Business (“CFIB”). When asked why they had not begun to prepare for their exit, 60% of business owners said it was “too early to plan for succession” (see figure 1.). On the contrary,

experts will tell you the lack of adequate time to plan and execute succession is one of the main reasons that successions fail.

An important step in kick-starting your succession plan can be to get past the mentality that ownership of the business and operational control of the business are one in the same. In my experience, many SME owners feel they need to hold the largest stake in the company in order to stay in the operational chair. The fact is that most business owners are very experienced in their field and very good at what they do, so they deserve the right to play a very valuable operational role in the future of the business - even if they do not own 100% of the business until the day they leave.

To coin an unfortunate phrase, a lot of business owners want to “die at their desk”. While you can't fault their dedication to the job, you do have to question the long-term benefits. If you retain full operational control and full ownership until the day you leave, what is there left in terms of a business legacy once you hand it over? Do you expect the successor to start from scratch all over again? Continuity in a business should be a primary concern. After all, you may want to retain an interest or collect ongoing dividends from the business even after you leave.

Consider Phasing Out Your Involvement

There are many benefits of involving the operational successor – whether that is a family member, part of the existing management group or an outside interest – well before you leave the business. That way you will have time to groom a successor to ensure a smooth transition upon operational hand over.

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An approach that can be very beneficial to all parties involved is what I'd call a “phased exit” or “partial buyout” where a new ownership group comes in and provides capital to your business and takes a minority equity stake. It's also an opportunity to liquidate some of your years of hard work and take some of your risk out of the business while retaining operational controls.

You may have plans to grow your business further in an effort maximize its value before you retire, but you're probably not willing to put your entire retirement fund at risk to do so. By bringing in a new financial partner, you are not only taking some of your risk off the table, but you are also potentially introducing new skills, possibilities and strategies that could help drive your business to the next level.

Even if you don't have a successor in mind (only half of the current SME owners that have a succession plan have actually chosen their successor) the right financial partner can also assist in that respect. If you select a group with a strong business network, they should be able to help you find the right person, or management team, to keep your business running successfully.

Choosing the Right Financial Partner

So you can see the benefits of phasing out your ownership stake and operational involvement in your business, but who can help you realize that goal? Private equity groups and banks are obvious financial candidates. Qualities that you might want to consider when selecting a financial partner include:

- An understanding of your industry
- A focus on, and commitment to, businesses of your size
- A strong strategic network, including potential successors and corporate financiers
- Access to capital and ability to offer flexible financing options
- Experience in negotiating the ultimate sale of a business

At the end of the day, you want a partner that will take the time to understand your long-term goals and not try to squeeze you and your business into the way that they do things. The right financial partner will help you strike the right balance between ownership and operational succession.



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