Succession Planning - Taking Inventory / Crucial Conversations

Dick Wittman, Wittman Consulting

Biosketch

- Ag Lender – FCS (1972-1980) – Spokane, WA & Washington, DC
- Partner in 20,000 acre diversified family farm business (1980-present)
  - New title – Jan. 1, 2017 – Board Chairman/Transition Coach
- Farm management consultant (1980-present)
  - Farm family transitions and formalization of governance structures, financial planning, managerial accounting, process improvement, consultant training
- Industry boards/affiliations
  - Farm Financial Standards Council – Past President
  - PNW Direct Seed Association – Director, Past President
  - Director – numerous commodity group and bank boards
  - Faculty member – TEPAP Program (fin mgmt. & process improvement), Texas A&M King Ranch Institute (MA)

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Transition Events

- 1980 – began ownership transition with stock transfers and contract buybacks
- 1983-85 – senior owners retired; completed buyout contracts
- 1987 – brother disabled/divorced; executed buyout
- 1994 – retired 3rd uncle & executed buyout; added two new partners to labor and ownership team
- 2000 – final payments on LT buyouts from off farm cousins
- 2007 – nephew joined management & ownership team
- 2008 – bought out partner (brother) who resigned
- 2009 – next phase of ownership transition to younger partners
- 2013 – retirement/buyout of major partner; expanded junior partners’ roles and investment levels.
- 2015/16 – Transition #10 underway—Getting the old goat retired!!!
Proverbial Wisdom

“It will never work. These family deals never last.”

Destiny ... or Choice?

Get your hankie out!

• Is professional management/communication “necessary evil”... or “critical asset” for family business viability & continuity?

• Tragic stories ... “Predictable Surprises”
  • Mom & dad with 4 sons and a dream of succession
  • 2 cousins with under-utilized expensive combines
  • $150,000 in attorney fees to split the sheets
  • Cousins - cattle dispute/shootout - 2 dead
  • $600,000 in lost efficiency to divide partnership
  • Grandkids at farm sale closing

Wittman’s Rule:
For transitions to be successful... there must be alignment of expectations!

Agenda - Succession Planning

• Taking inventory of your current personal and business situation
• Defining and executing critical conversations that must take place among key stakeholders
• Identifying issues where action is needed and formulating alternative scenarios for execution
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
  - 90% fail to pass to the third generation

#1 Conclusion
(after 36 years of working with farm businesses)

- 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 Batterson, The Circle Maker*

Describe how your business is managed TODAY.

Successors need to know what they’re getting into.
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

Should this be everybody’s goal?
Story: father & 2 sons
Operating Philosophy/Core Values Statement (excerpts)

- Strive for excellence
- Be early adapters
- Committed to professional management
- Open and professional communication
- Environmentally conscious methods
- Quality records openly shared

Wittman’s Rule:
For transitions be be successful... **there must be alignment of expectations!**

How do you score?

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 – “Entitlement rules!”
  - Pay and position should be based on skills and performance

Vision & Core Values
Consequences of “Bad Chemistry” and Lack of Consensus

- 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
“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

- Goals (28% do this)
  - Get them on paper – don't need to be fancy
  - Personal & Business
  - Identify stakeholders intentions & wishes
  - Dispel myths and erroneous assumptions
  - Plan your family meeting to do this!
- Action plans
  - What, When, Who
  - Budgets, Cashflows
  - Resources required
  - Feasibility
Lack of Professional Planning
...consequences

• 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!**

**Management System Model**

- Establish Mission, Vision, Core Values
- Plan
- Organize/Divide Responsibility
- Set Policies & SOPs
- Communicate & Coordinate Efforts
- Implement Plan
- Establish Controls
- Measure Performance
- Adjust Plan

Who should be on the 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?
  - Duty statements review, timetables for transition, apprenticeships, OJ training
• How does old guard get out of the way?
  - Board chairman vs. CEO (“boss”)

**Have you tried this at home?**

What does your organizational structure look like?
Why Write Job Descriptions?

...you can’t delegate what you can’t define!

- 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 focus on key decisions of exiting member
  - Checklist for training, delegation, and validation
- 36 DUTIES listed in Guidebook

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, control systems
- Execute contracts
- Provide information and policy input to board of directors

What if successors are technicians & operators?
Avoid “Bossing Tendency”
Define Attributes of Ideal Manager

• 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”

Rain break weaning calves

From: Grandpa, Grandma and Me by Stuart Hample & Eric Marshall

Job Description - Board Chairman

• 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

Management System Model

[Diagram showing steps in management system: Establish Mission, Vision, Core Values, Plan, Organize/Divide Responsibility, Set Policies & SOPs, Adjust Plan, Measure Performance, Establish Controls, Communicate & Coordinate Efforts, Implement Plan]
Policies and Practices

Do policies and SOPs attract and retain successors? 

...OR chase them away?

Are Policies Written Down? 
...Common “Land Mines”

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

36% do! 

Ask each member of farm management team to write down understandings...then compare notes. (see Questionnaire)

Compensation Summary 

<table>
<thead>
<tr>
<th>Name: Joe Owner-Operator</th>
<th>Year: 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Salary</strong></td>
<td><strong>Rate/Mo</strong></td>
</tr>
<tr>
<td>Nov-Feb</td>
<td>$2,000</td>
</tr>
<tr>
<td>Mar-Oct</td>
<td>$0.00</td>
</tr>
<tr>
<td>Cash Salary &amp; Wages Subtotal:</td>
<td>$24,000.00</td>
</tr>
<tr>
<td>Social Security Benefit - % Rate:</td>
<td>7.65%</td>
</tr>
<tr>
<td><strong>Housing</strong></td>
<td><strong>Rate/Mo</strong></td>
</tr>
<tr>
<td>$1,000.00</td>
<td>12</td>
</tr>
<tr>
<td><strong>Utilities - Power, Phone,auto</strong></td>
<td><strong>Rate/Mo</strong></td>
</tr>
<tr>
<td>$300.00</td>
<td>12</td>
</tr>
<tr>
<td><strong>Meal Allowance, Groceries</strong></td>
<td><strong>270 days @ $6.00/day</strong></td>
</tr>
<tr>
<td><strong>Beef, Farm Produce</strong></td>
<td><strong>1/2 beef - 350# @ $1.40/lb</strong></td>
</tr>
<tr>
<td><strong>Other-</strong></td>
<td><strong>Rate/Mo</strong></td>
</tr>
<tr>
<td>$200.00</td>
<td>12</td>
</tr>
<tr>
<td><strong>Medical Insurance</strong></td>
<td><strong>Rate/Mo</strong></td>
</tr>
<tr>
<td>$450.00</td>
<td>12</td>
</tr>
<tr>
<td><strong>Uncovered Medical Reimbursement</strong></td>
<td><strong>Rate/Mo</strong></td>
</tr>
<tr>
<td>$0.00</td>
<td>12</td>
</tr>
<tr>
<td><strong>Other-</strong></td>
<td><strong>Commuting Pickup</strong></td>
</tr>
<tr>
<td>$3,000.00</td>
<td>12</td>
</tr>
<tr>
<td><strong>Other-</strong></td>
<td><strong>Auto Insurance, gas, maint- -Spouse &amp; children</strong></td>
</tr>
<tr>
<td>$0.00</td>
<td>12</td>
</tr>
<tr>
<td><strong>Total Wage and Benefits Value</strong></td>
<td><strong>Rate/Mo</strong></td>
</tr>
<tr>
<td>$55,946.00</td>
<td>12</td>
</tr>
<tr>
<td><strong>Bonus- Based on Year End Results</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Retirement Contribution @</strong></td>
<td><strong>Rate/Mo</strong></td>
</tr>
<tr>
<td>7%</td>
<td></td>
</tr>
<tr>
<td><strong>Total Compensation:</strong></td>
<td></td>
</tr>
</tbody>
</table>

Non-Taxable Benefit Analysis @ Tax Rate: 
43.15% 30.15%

Pre-Tax Wage Equivalent $60,000 $48,833
Total Tax Savings $25,890 $14,723

Tot. Pre-Tax Wage Equivalent $81,836 $70,669

- " " " " - Per Hour $32.73 $28.27

Tax Table Summary 

<table>
<thead>
<tr>
<th>Federal Tax</th>
<th>High Rate</th>
<th>Low Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>26.60%</td>
<td>15.00%</td>
<td></td>
</tr>
<tr>
<td>State Tax</td>
<td>7.50%</td>
<td>7.50%</td>
</tr>
<tr>
<td>Social Security Tax</td>
<td>7.85%</td>
<td>7.85%</td>
</tr>
</tbody>
</table>

Do we appreciate the $ value of all the “bennies”? 
Are we giving our business $33/hour in labor value?
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
  ▫ Correlating compensation/bonuses with responsibility and performance
  ▫ Merit vs. paternalism as criteria for hiring and advancement
  ▫ Avoiding discrimination - family vs. non-family employees/owners
  ▫ Policies on pre-nuptials

“...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 at 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

Family Business Investment and Equity Withdrawal Policy

Components of Policy

- Who is welcome to invest in farm/ranch?
- Waiting period to become an investor?
- Should everyone be equal?
- Minimum capital to leave invested? “Can I ever get my money out?”
- Is revenue sharing tied to ownership ratios?
- Compensation for excess balances?
- Who monitors capital balance compliance with legal agreements?

Stories…Australian & Montana partnerships

(See Wittman Guidebook – Chapter 6 – Sample Templates)
Communication 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%

What's your DiSC dimension?

Management System Model

Establish Mission, Vision, Core Values
Adjust Plan
Measure Performance
Establish Controls
Communicate & Coordinate Efforts
Plan
Organize/Divide Responsibility
Set Policies & SOPs
Implement Plan

Management Control System Key Elements

• Comprehensive Financial Record Review Process
• Regular Performance Reviews – Individual & Farm Business
• Ongoing Training & Professional Development
• Use of Outside Advisers
• Good audit and internal control systems

"We manage what we measure."
"People do what is INSPECTED, not what is EXPECTED!"
Sharing Financials with Successors

- Do you understand your wealth position?
  - Cost and market basis; deferred tax, etc.
- Have you shared your position with successors?
  - If yes, how did it go?
  - If no, what are your fears?
- Stories of successful attempts...

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?
Can professional feedback change behavior???

- 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
- Succession challenge:
  - Transfer from PARENTING
  - To mentor, coach, supervisor
Goals of Today’s Comments

- Identify critical conversations & issues
- Show path to
  - Build knowledge for yourself and advisory team
  - Implement professional governance structures & transition plans

“Fireman Story…”

Where to start? TEPAP Participant

- Appoint Transition/Governance Development Coordinator or Task Force
- Assemble transition advisory TEAM
- Map out transition steps and management process needing clarity
- 3 D’s – Discuss, decide and document
- Join peer networks
  ...most important: deal with Succession Issues, THEN Estate Planning issues

Succession Planning

- Starts with “mission, vision, values talk”
  - Business continuation or liquidation?
  - Management and ownership transition
- Deals with who will be involved, tactics, timing, legal agreements (buysouts), duty transitions, family employment policy, compensation, etc.
  ✓ “Business Life Planning”

Estate planning

- Financial Wealth analysis - estate tax risk; liquidity coverage; insurance needs
- Capacity to provide retirement security
- Capacity to distribute wealth - now vs. later
- Investment strategies - post retirement
- “Death Planning” - final instructions, distribution of personal assets, health care
Building Collaborative Team

• Assess current local advisory team; is outside facilitation needed?
  ▫ What is your family communication culture?
  ▫ Technical knowledge of group?
  ▫ Potential conflicts of interest?
• Establish ground rules ... this is TEAM sport!
• Be on guard for “the sale” vs. advice & counsel; be willing to invest in the process

Advisory Team Candidates

• Accountant
• Attorney
• Insurance Agent
• Wealth Management/Investment Advisor
• Banker
• Trust Officer
• Pastor
• Facilitator

Building family & business profile

Ask: What do you & advisory team need to “take inventory...” (start with 3-ring binder)

• Biographical information – resumes, family information, BD, addresses, goals, personality profiles
• Business Profile
  ▫ History of the business - narrative
  ▫ Governance
  ▫ Tax returns, financial position & trends
• Insurance coverages
• Estate plan documents, wills, trusts, POA, etc.

How much are we paying professional advisors to accumulate this information?
**Favorite Reads**

“Getting to Yes: “Crucial Conversations” - Patterson, Grenny
“Negotiating Agreement Without Giving In” - Fisher and Ury
“Perpetuating the Family Business” - John Ward
“Good to Great” - Jim Collins
“The Enduring Legacy: Essential Family Business Values” - Lance Woodbury
“I’m Stuck, You’re Stuck” - Tom Ritchey
“Farm Business & Estate Planning” - Neil Harl
Family Business Magazine - FBM

Make “knowledge building” in family business excellence a lifetime journey.

**Time for Questions**

**Further Information:** www.wittmanconsulting.com
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- Seminars & Consultant Training information