NE167R Concept Paper

Succession Issues - B45, B46, B47

4/98

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Relevant literature addressing family succession/transfer issues in family-owned businesses follows
Initial Recommendation: Goodman

Goodman, J. M., & Dreux, D. R., IV (1997). Business succession planning and beyond: A multidisciplinary approach to representing the family-owned business. American Bar Association.

It is increasingly evident to many professional service providers, educators, researchers, legislators, trade associations, community leaders, corporate entities, and governmental agencies that family-owned businesses (FOBs) are not only a significant global phenomena, but, perhaps more importantly, also constitute the fundamental organizing unit of both society and commerce. Indeed, aw the academic community continues to apply time and scrutiny to the field, it becomes ever more apparent that family business, which inevitably has it origins in home-based business, is merely the wider-lens view of entrepreneurial activities in general, inasmuch as it encompasses the origins, relationships, values, and issues of the owner/manager system as well as the actual commercial activities of the enterprise itself. Family business is the "complete" picture. With this in mind, let us begin at the beginning.

assets strategies vs personnel strategies
Kaye framework

Variable Name	Question Asked	Card #	Variable # in code book
	Dependent variable		
YESNO	There are many ways that family business owners might plan for leaving the business due to retirement or other circumstances. Please tell me if you have done any of the following: (a) through (f). Added up indices.	6	B45
	Independent variables		
DEBT	What were the total liabilities, including debt, as of December 31, 1996	5	B36
FIVEYRCH	During the next five years, do you expect the ownership of [business Name] to change?	6	B47a Note
HEALTH	How would you rate your overall health?	6	B48
HOWINVOV	How did you first get involved in the business? Note: If 2: inherit the business from a relative, recode as 1, otherwise, recode as zero.	3	B6
LENGTH	How old were you when you first started working in [Business Name]? Note: LENGTH variable is obtained by "1996-this number."	3	B7
PERCEOWN	What percentage of the business did you own as of December 31, 1996?	5	B32
PLAN	Please indicate to what extent each activity is part of your business's regular practices by using a scale from 1 to 5, where 1 means the activity is not done at all and 5 means the activity is done to a very great extent at your business: j. Developing or updating a written strategic plan, including a mission statement	5	B15(j)
PROLOSS	What was the profit for this business in 1996? Code profit or loss.	5	B31
WAYINCOM	We would like to know how you would describe yourself as a business person. Think of a scale from 1 to 5, where a 1 means that for you the business is a way of life, and a 5 means that for you the business is only a way to earn income.	5	B19a
GENDER		7	1bb

Variable Name	Question Asked	Card #	Variable # in code book
	Dependent Variable		
SECURITY	People who plan to transfer ownership of their family business upon retirement or death deal with a variety of issues. Please tell me how important of providing financial security for yourself or your survivors is in transferring ownership of the business?	6	B46c
	Independent Variables		
PROFIT	What was the profit for this business in 1996? Profit/Loss	5	B31
FAM1	Is "a secure future for younger family members" the most important long-range goal for your family?		B27(4)
FAM2	Is "secure retirement resources" the most important long-range goal for your family?		B27(5)
CASHFL	During 1996, how often did the business have a cash-flow problem?	5	B39
PERCOWN	What percent of the business did you own as of December 31, 1996?	5	B32
GENDER		7	1bb
RACE	What is your race?	6	B49

Variable Name	Question Asked	Card #	Variable # in code book
	Dependent Variable		
YESNO	If respondent has developed a written plan to transfer the ownership of the family business before you retire or die	6	B45(e)
	Independent Variables		
DEBT	What were the total liabilities, including debt, as of December 1, 1996?	5	B36
FIVEYRCH	During the next five years, do you expect the ownership of [business name] to change?	6	B47a
HEALTH	How would you rate your overall health?	6	B48
HOWINVOLV	How did you first get involved in the business? <u>Note:</u> If 2: inherit the business from a relative, recode as 1, otherwise, recode as zero	3	B6
LENGTH	How old were you when you first started working in [business name]? <u>Note:</u> LENGTH variable is obtained by "1996-this number."	3	B7
PERCEOWN	What percentage of the business did you own as of December 31, 1996?	5	B32
PLAN	Please indicate to what extent each activity is part of your business's regular practices by using a scale from 1 to 5, where 1 means the activity is not done at all and 5 means the activity is done to a very great extent at your business: j. Developing or updating a written strategic plan, including a mission statement.	5	B15(j)
PROLOSS	What was the profit for this business in 1996? Code profit or loss.	5	B31
SUCCESS	Overall, how successful is your business to date?	5	B18
WAYINCOM	We would like to know how you would describe yourself as a business person. Think of a scale from 1 to 5, where a 1 means that for you the business is a way of life, and a 5 means that for you the business is only a way to earn income.	5	B19a
GENDER		7	1bb

Ambrose, D. M. (1983). Transfer of the family-owned business. Journal of Small Business Management, 21, 49-56.

Federal policy and managerial assistance programs have devoted much attention to the creation of entrepreneurial business ventures. However, each year great numbers of businesses are terminated. One cause is the conclusion of ownership by one generation and the failure of the following generation to assume ownership. Attempts to perpetuate family-owned businesses might provide a greater aggregated impact on small business survival than the laborious attempts to create new businesses. The intent of this research was to identify and evaluate those factors which encourage and those which inhibit the effective transfer of ownership of the family-owned business.

Anon. (1998). Estate planning: It gets better all the time. Fortune, 137(5), 178.

Take advantage of improved ways to protect your estate—or your heirs could face a 55% tax.

Barnes, L. B., & Hershon, S. A. (1976, July-August). Transferring power in the family business. Harvard Business Review, 54(4), 105-114.

Should a family business stay in the family? The question is really academic, since families appear to be in business to stay. But, when the management moves from one generation to the next, the transition is often far from orderly. In addition, as the company develops, there is a need for a management style that goes beyond survival thinking, and entrepreneurs tend not to be reorganizers. In fact, while a sometimes bitter power struggle is peaking, the fortunes of the company may be sliding downhill. In other cases, power struggles are part of a healthy transition. According to these authors, family and company transitions will be more productive when they are simultaneous. The external problem involves the older generation's making use of the flexibility and new ideas of the succeeding generation. Third party involvement may help to prevent irreparable family rifts and company stagnation. Dialogues between all the parties—managers, relatives, employees, and outsiders—can also help.

Beckhard, R., & Dyer, W. G., Jr. (1983, Spring). Managing change in the family firm: Issues and strategies. Sloan Management Review, 24(3), 59-65.

Although family-owned firms constitute a large portion of corporate America, they face unique problems that are rarely discussed. In this paper, the authors outline key issues that they feel an owner of a family-owned firm must address in order to avoid losing control of the business. They also make suggestions for those families who want to retain control of their companies through succeeding generations.

Beckhard, R., & Dyer, W. G., Jr. (1983, Summer). Managing continuity in the family-

owned business. Organizational Dynamics, 12(2), 5-12.

Perpetuating a family business when the founder retires or dies calls for careful planning by the founder, the family, and the firm's key professionals.
In this article we will look at the critical issues and dilemmas that face founders and second-generation "founders" and provide a perspective for thinking about a family-owned business as a complex system that includes the subsystems of family and firm and the interactions between them.

Berolzheimer, M. G. (1980, January-February). The financial and emotional sides of selling your company. Harvard Business Review, 58(1), 6-11.

Because many large corporations are on a constant lookout to acquire fast-growing private companies, owners of such companies usually have frequent opportunities to sell out. Sometimes the owners have valid reasons for wanting to sell. These reasons can include changes in markets, technology, resources, capital requirements, and management loyalty. Of equal or greater importance are personal factors such as the owner's age, career aspirations, and marital situation, along with the existence of heirs to take over the business. Once a decision is made to sell, the owner faces a thorny problem: how to arrange the sale. This issue's *Growing Concerns* feature consists of one company owner's personal account of the sale of his company. He explores first how he came to the decision to sell and then how he negotiated the sale.

Birley, S. (1986, July). Succession in the family firm: The inheritor's view. Journal of Small Business Management, 36-43.

Much has been written about the issue of succession in the family firm, and about the heartaches and feuds which often follow. Most writers, however, have taken the perspective of the incumbent—the current owner. In this paper the issue will be examined from the viewpoint of the children who inherit the business.

Blattmachr, J. G., & Zaritsky, H. M. (1997). Estate planning after the Taxpayer Relief Act of 1997. Journal of Taxation, 87(3), 133-147.

A host of changes relating to income, gift, estate, and generation-skipping transfer taxes will require the immediate review of most estate plans. Some of the provisions that have received the most attention from the general press, such as the increase in the exclusion and relief targeted to family-owned businesses, may not have as great an impact as lesser-known charges such as the new charitable remainder trust rules.

Burack, E. H., & Calero, T. M. (1981, January). Seven perils of the family firm. Nation's Business, 62-64.

The idea of running a family business is appealing. Be your own boss. Set your own pace. Keep the rewards. Not so appealing but equally real, however, are the many risks that can lead to disaster. What follows are seven potential problem areas a family business may face and some advice on how to avoid these common pitfalls.

Corneel, F. G. (1997). The electing small business trust: Subchapter S's user-friendly estate planning tool. Journal of Taxation, 87(3), 215-223.

The availability of the electing small business trust creates significant estate planning options for S corporation shareholders. Although questions remain concerning the tax treatment of distributions, taxpayers nevertheless may apply various approaches to take advantage now of the undoubted benefits of these trusts. Still, because the precepts relating to ESBTs are not yet clearly established, the trusts' governing instruments should allow for amendments as necessary in light of changing tax rules and other factors.

Davis, S. M. (1968). Entrepreneurial succession. Administrative Science Quarterly, 13, 402-416.

This paper examines three patterns of entrepreneurial succession in private enterprise in developing countries. The process may be thought of as the succession from entrepreneurs to executives. The findings suggest significant variation in the adaptability of each type to the development of modern organizations in which the *function* of management is distinct from the manager as a *person*.

Horton, T. R. (1982, July). The baton of succession. Management Review, 2-3.

As the CEO elected to succeed Jim Hayes, I have benefitted from his example of inspired leadership. It seems appropriate, therefore, to build on his theme of succession by spotlighting the concerns and responsibilities of an incoming manager during the transition period. What are the tasks of first priority? In charting a course for the future, how can an organization's momentum be maintained....its values preserved....its opportunities exploited to provide a sense of direction for the future? How can the human and organizational need for continuity be balanced against the compelling requirements for change?

Kessel, E., & Petkun, L. B. (1996). Are Crummey withdrawal rights still a viable estate planning tool? Journal of Taxation, 85(3), 146-150.

The major taxpayer victory in *Estate of Crisofani* has apparently spurred the Service into launching a new attack on annual exclusions claimed for gifts in trust where the beneficiaries have *Crummey* powers. The rationale applied by the IRS in a recent ruling appears contrary to the interpretation given by the courts, and, in some instances, by the IRS itself to the application of *Crummey.*

Rasmussen, C. J. (1986). The sexual politics of estate planning in Wisconsin: An introduction to the marital property act. Real Property, Probate and Trust Journal, 21(3), 485-525.

Wisconsin's Marital Property Act became effective January 1, 1986. This article describes the Act, compares it to the Uniform Marital Property Act, and discusses several issues it raises.

Rollock, A. C. (1998). Professional responsibility and organization of the family business: The lawyer as intermediary. Indiana Law Journal, 73, 567-587.

Lawyers are often called upon to represent multiple clients in organizing businesses. Such representation may include advice as to the appropriate form of business entity, capitalization, internal governance, and, in the case of family businesses, estate planning. In many of these situations, the parties have already reached a preliminary agreement as to the general structure of their investment in the enterprise, and they wish to minimize the legal costs associated with starting the business. Although the representation of multiple clients by a lawyer acting as an "intermediary" between or among clients with potentially conflicting interests has gained widespread acceptance in the profession, the benefits of such representation to each client do not necessarily outweigh the costs to the client occasioned by the lawyer's divided loyalty. This is particularly true in the case of a family business. The existence of a familial relationship may contribute to a failure by the lawyer and/or clients to recognize or fully appreciate the potentially conflicting interests of the family members. Moreover, current trends with respect to the creation of new forms of business entities and the recent adoption by the IRS of its "check-the-box" regulations will require lawyers to reexamine not only the advice that they render with respect to which type of business entity is most appropriate for a given business enterprise, but also whether the attorney may ethically represent all or some of the owners in organizing that business.

Russell, C. S., Griffin, C. L., Flinchbaugh, C. S., Martin, M. J., & Atilano, R. B. (1985). Coping strategies associated with intergenerational transfer of the family farm. Rural Sociology, 50(3), 361-376.

Five strategies for coping with the stress created by the intergenerational transfer of the family farm were identified in a population of Midwestern families. These strategies were then associated with measures of psychological well being and perceived ease in making the farm transfer decision. Parents had higher psychological well being than their children, even though fathers reported the transfer decision to be somewhat more difficult than did sons. Use of family discussion was positively associated with well being for fathers. Daughters-in-law were especially lacking in effective coping strategies.

Schwartz, E. L. (1954, September-October). Will your business die with you? Or will you take the time now to save a lot of trouble later? Harvard Business Review, 110-122.

Who is going to die first—you or your business? How will that death affect the business? How will it affect the welfare of your family? What are the business, legal, tax, and insurance problems involved? Are they simple, or are they complex?

Trow, D. B. (1961). Executive succession in small companies. Administrative Science Quarterly, 6, 182-239.

The main focus of this paper is on factors that influence how well prepared an organization will be for succession in its top positions. Data are drawn from cases of imminent or completed succession in over one hundred small manufacturing companies. In these companies, the main factors influencing planning and subsequent profitability appear to be the availability and competence of a family member as successor. Their influence appears to operate mainly through their effects on the timing of the succession-planning process.

Ward, J. L. (1990, Winter). The succession process: 15 guidelines. Small Business Forum, 8(3), 57-62.

Succession is the most painful and critical time for family businesses. Less than one-third of family businesses survive into the second generation, and only about 13 percent make it into the third generation. How do the successful ones make it? After working with hundreds of family businesses, I'd like to offer 15 guidelines that I hope will help you during the succession process.

Yates, R., Langbein, J., Dobris, J., Schneider, P., Zartman, J., Waggoner, L., Baker, J., Plaine, L. L., & Goodman, M. R. (1991). Estate planning for the '90's: A discussion. ABA Journal, 77, 60-64.

There is much less expectation of traditional inheritance. Children expect help with educational expenses, but thereafter the parents feel free to consume their wealth.