HOW TO PLAN FOR SUCCESSION: **PAVING THE WAY FOR CONTINUED PROSPERITY**

Proficient chess players begin each game with a clear strategy that prepares multiple moves in advance. While each move is designed to set up the next, a strategic chess player will remain adaptable to changing circumstances. This same approach of strategic forethought, flexibility and responsiveness are best practices for succession planning in wealthy families as well.

TRANSITIONING LEADERSHIP AND MANAGEMENT

Succession will happen—it's a matter of when, not if—so families should prioritize proactive planning to ensure a smooth, successful transition. Data highlights the consequences of inadequate succession planning: Although **more than 30%** of family-owned businesses transition successfully to the second generation, **just 12%** of those businesses are viable for the third generation, and **a mere 3%** are operating by the fourth generation, according to *Family Business Review*.

There are many aspects to robust succession planning, which, when done well, can help align decision-making and strengthen family unity. The succession plan should address transitioning both the **ownership and control** of the family wealth enterprise as well as the **leadership and management** of the family office and, if applicable, the business too. We addressed ownership and control concerns in our previous insight—How to Plan for Succession: Preserving, Protecting and Passing on Wealth—and here we focus on the equally important elements of leadership and management succession.

There are several key factors when transitioning leadership and management, and while the required skill sets will vary depending on the specific roles, the necessary considerations are similar. Diligent and nimble succession planning helps pave the way for continued prosperity in the family wealth enterprise. We've identified three different scenarios that encompass most transitions, but the decision-making about succession varies in significant ways across those scenarios.

CENTRAL CONSIDERATIONS FOR LEADERSHIP AND MANAGEMENT ROLES

The family wealth enterprise has three interconnected circles of participation—the family members, the family's business and the ownership of wealth—and each circle has a distinct lifecycle, but these lifecycles may not always correspond. That's why having a detailed succession plan is so critical.

There are several key factors to consider when transitioning leadership and management, and while the required skill sets will vary depending on specific roles, the necessary considerations are similar. For example, when planning for succession, the person taking on ownership and leadership roles may be the same individual, but often times they are not. Overall, the plan must outline how to assess a candidate's characteristics in two main areas: interpersonal skills and professional experience.

HOW TO PLAN FOR SUCCESSION: PRESERVING, PROTECTING AND PASSING ON WEALTH

The key to success is to be thoroughly prepared. Succession will happen within families, but it is not always certain that it will be accomplished strategically. Succession planning calls for deliberate preparation, and it requires time—typically years or even decades—as well as forethought, commitment, diligence and adaptability.

TRANSITIONING OWNERSHIP

The decisions made regarding ownership of the family office or closely-held business may not necessarily be the same decisions that are required for leadership and management. It's critical to understand and acknowledge the different elements that proper succession planning entails.

The family wealth enterprise has three interconnected circles of participation—the family members, the family's business and the ownership of wealth—and each circle requires a succession plan. Those plans should reflect the family's shared values and aspirations, and they should be implemented with business-like focus and diligence that is tailored to each family's dynamics and relationships.

To successfully transition the family ownership, business and financial wealth to succeeding generations, leaders must be groomed and/or nurtured to assume the mantle of these responsibilities with competence. Moreover, to ensure that the family legacy remains intact and on course, each person assuming a new role must embrace the family's common vision. Outlining deliberate plans to accomplish related goals across the family, business and ownership will help achieve an orderly, prosperous succession that protects the family legacy for generations to come.

WHAT IS SUCCESSION PLANNING AND WHY IS IT SO IMPORTANT?

Robust governance practices form the cornerstone of success for the family wealth enterprise, and ongoing succession planning is one element of a mature governance system. As a family considers its future succession, it is vital to understand why a well-conceived plan is so important and what the critical elements of the plan entail. The succession plan prepares heirs to transition successfully and preserve, grow and pass wealth from generation to generation. Otherwise, the family wealth enterprise can diverge from the family's values, philosophies and direction, which may erode family unity, endanger the legacy and dissipate financial wealth.

Learn more about governance: Effective Governance Strengthens Family Unity and Builds a Lasting Legacy.

Learn more about transitioning ownership: How to Plan for Succession: Preserving, Protecting, and Passing on Wealth

Scenario #3: There Is No Heir and the Family Must Decide About the Future

Sometimes, for a variety of reasons, there is no heir identified or available to fill the role. Then it may be necessary to select a non-family individual as a successor for long-term leadership and management. If so, the family will still want to retain ownership and control while also ensuring continuity for ongoing success.

In this case, the process will be similar to identifying an executive candidate in a business. It requires a clear description of the role and a defined set of expectations for the candidate to fulfill, but it's imperative for them to establish trust and confidence with the family and key stakeholders in the business. Clearly outlining their responsibilities, and confirming the experience and ability to carry them out, will prepare both the family and the candidate for success.

However, lacking an identified heir can trigger difficult decisions about the future of a family business. Selling the business or going public could be viable options, depending on the family's goals and circumstances, as well as the overall outlook for the business and industry. In some cases, ceding control may be the best way for family members to "cash out" and maximize value, but there are many options available, including tapping current non-family executives.

Bringing in non-public investors who can provide both capital and expertise can also help continue business operations, and their compensation can be structured in a way that avoids giving up equity and maintains full ownership. Particularly in this scenario, it's important to link compensation to business performance without yielding equity, and a phantom stock agreement is one way to achieve this. Ultimately, there is no single solution for this scenario, but deliberation among all key stakeholders will help to weigh the options and decide upon the best course to address the family's goals and values.

Leadership Compensation Considerations

Family Member
Compensation should be commensurate with the heir's skills, experience and performance relative to similar roles at other organizations.

Non-Family Individual
Compensation should be reviewed closely and subject to board approval.

Non-public Investors
Compensation can be structured to avoid giving up equity and maintain full ownership.

SCENARIO PLANNING FOR YOUR FAMILY

While the appropriate strategy for succession planning will depend on the individual situation, every plan and timescale must remain adaptable to changing circumstances. Building flexibility into the plan is critical to navigating unplanned external triggers, like an economic downturn, which may require reassessing the succession plan. A range of other disruptors can impact the plan, including industry-specific changes, new regulations, demographic shifts, technological advancements or even a public health crisis. Families may have to deal with unforeseen personal issues that arise too (e.g., divorce, health complications, death), so succession planning should have ample forethought along with recurring assessments. Even with the best-laid plans, remaining responsive and adaptive is invaluable.

The succession of leadership and management requires a long-term strategy, so families should think far beyond the next move. By preparing well in advance, identifying clear requirements for each role, providing ample training for necessary capabilities and remaining adaptable to shifting circumstances, families can protect their legacy and ensure ongoing success.

3 STEPS FOR LEADERSHIP AND MANAGEMENT SUCCESSION:

1. Set a clear and flexible strategy for transitioning leadership and management roles.
2. Have a contingency plan in place should circumstances change.
3. Outline directives for family and non-family successors, including personality traits, business acumen, responsibilities and compensation.

Learn more about how **BDO's Family Office Services** help families preserve, protect and pass on wealth. **Subscribe to our Family Office Newsletter** to receive curated insights relevant to family wealth enterprises.