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SPOTLIGHT ON:

Business succession planning

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STEPS TO SMOOTH BUSINESS TRANSITIONS

Planning for the future of your business is one of the most critical responsibilities of an owner. Business succession planning ensures your enterprise can transition smoothly to new ownership or leadership, safeguarding its continuity and success. Whether you're passing the reins to a family member, selling to a third party, or considering other options, taking proactive steps can protect the legacy you've built.

Here's what you need to know about business succession planning, why it matters, and how to make the process seamless.

WHAT IS BUSINESS SUCCESSION PLANNING?

Business succession planning involves preparing to transfer ownership, leadership, or control of your business. The aim is to ensure the company thrives after your departure, whether due to retirement, illness, or unforeseen circumstances.

It's not just about selecting a successor – it's about creating a roadmap that includes financial, legal, and operational considerations to help the transition run smoothly.

WHY IS BUSINESS SUCCESSION PLANNING IMPORTANT?

Failing to plan can lead to disruption, financial instability, and even the closure of your business. Research by the Federation of Small Businesses (FSB) shows that around 40% of UK business owners still need a succession plan. With over five million small businesses in the UK, this lack of preparation poses a significant economic risk.

Additionally, succession planning can:

- **Protect business value:** With a plan, your business could retain value during a transition. A clear strategy helps maintain operations and client trust.
- **Minimise tax liabilities:** Proper planning can help mitigate inheritance tax or capital gains tax liabilities, which can otherwise create a financial burden.
- **Ensure continuity:** Planning reduces the risk of operational disruption and preserves relationships with clients, suppliers, and employees.
- **Prepare for the unexpected:** Life is unpredictable. Having a plan means your business is better equipped to weather sudden changes.

EXPLORING SUCCESSION OPTIONS

Deciding how to transition your business is as important as preparing for the process. Here are the most common paths for business succession, along with their pros and cons:

FAMILY SUCCESSION

Handing your business to a family member can be a natural choice, especially in family-run enterprises. It allows the business to remain within the family and continue a legacy. However, assessing whether the family member is interested and capable of taking on the role is essential. Misalignment in goals or an unprepared successor can lead to conflict or instability.

SELLING TO A THIRD PARTY

Selling your business to an external buyer can maximise financial returns, especially if your business has significant market value. Preparing for a sale involves ensuring clean financial records, demonstrating consistent profitability, and presenting growth opportunities. The challenge lies in finding the right buyer who aligns with your values and ensuring the transition doesn't disrupt operations.

MANAGEMENT BUYOUTS (MBOS)

An MBO allows key employees or management team members to purchase the business. This option ensures continuity since the buyers already understand the business. However, funding an MBO can be complex, requiring the management team to be financially capable of taking ownership.

EMPLOYEE OWNERSHIP TRUSTS (EOTS)

EOTs are becoming increasingly popular in the UK. This structure allows employees to collectively own the business collectively, fostering a sense of shared responsibility and commitment. EOTs can also provide tax advantages, such as exemption from capital gains tax on qualifying sales. However, transitioning to an EOT requires careful planning and financial structuring.

Misalignment in goals or an unprepared successor can lead to conflict or instability.

THE STEPS TO EFFECTIVE SUCCESSION PLANNING

STEP 1: DEFINE YOUR GOALS

Start by thinking about your objectives. Do you want to pass the business to a family member, sell to a third party, or transfer ownership to employees? Your decision will influence the entire plan, so it's crucial to have clarity from the outset.

STEP 2: ASSESS THE VALUE OF YOUR BUSINESS

Understanding your business's worth is essential, especially if you plan to sell. A professional valuation will provide a clear picture of its financial standing and potential market value. When valuing your business, consider intangible assets like your brand reputation, customer loyalty, and intellectual property. These elements often hold significant value but can be overlooked in traditional valuations.

STEP 3: IDENTIFY POTENTIAL SUCCESSORS

Choosing the right successor is one of the most critical decisions in the process. If you're transferring to a family member, consider their skills, interests, and readiness to lead. Identify suitable buyers who align with your company's values and goals for external sales. Developing a shortlist of successors and investing in their leadership development may also be helpful. For example, enrolling them in external training programs or providing mentoring can ensure they're prepared to take on the role.

STEP 4: DEVELOP A TRANSITION PLAN

Once you've identified your successor, create a detailed transition plan. This should include:

- **Training and mentorship:** Ensure your successor has the skills and knowledge needed to lead effectively.
- **Operational handover:** Define how and when responsibilities will transfer.
- **Financial arrangements:** Outline the structure of the sale or transfer, including any payment terms or retained interests.

STEP 5: REVIEW LEGAL AND TAX IMPLICATIONS

Succession planning involves complex legal and tax considerations. Work with professionals to ensure compliance and minimise liabilities. Key areas to address include:

- **Inheritance tax:** Transfers of business assets may qualify for relief under Business Property Relief (BPR).
- **Capital gains tax:** The sale of your business could trigger CGT. While Entrepreneurs' Relief (now Business Asset Disposal Relief) currently reduces the rate to 10% for qualifying individuals, this is set to increase to 14% from 6 April 2025 and 18% on 6 April 2026. Factoring in these changes is crucial to optimise your tax position.
- **Shareholder agreements:** If your business has multiple owners, ensure agreements are in place to manage ownership changes.

STEP 6: COMMUNICATE THE PLAN

Transparency is vital. Share your plan with key stakeholders, including family members, employees, and advisers. Clear communication reduces misunderstandings and ensures everyone is on the same page.

STEP 7: MONITOR AND UPDATE THE PLAN

Succession planning is not a one-time task. You should regularly review and update your plan to reflect changes in your business, industry, or personal circumstances.

THE BENEFITS OF STARTING EARLY

Procrastination often leads to rushed decisions and missed opportunities. Starting early offers significant advantages:

IMPROVING SUCCESSOR READINESS

By planning well in advance, you can dedicate time to training your successor. Leadership coaching, on-the-job experience, and professional development programs contribute to their readiness for the role.

ATTRACTING BETTER BUYERS

If you're selling your business, a well-prepared succession plan increases its appeal to buyers. A structured plan demonstrates professionalism, minimises risks, and can even boost the sale price.

TAX ADVANTAGES OVER TIME

Tax planning benefits from longer timelines. For example, spreading the ownership transfer across multiple years can reduce tax liabilities or provide more opportunities to take advantage of reliefs like Business Property Relief or Entrepreneurs' Relief.

COMMON CHALLENGES IN SUCCESSION PLANNING

Many business owners need more time for succession planning due to its complexity or emotional nature. However, addressing these challenges early can make the process easier.

- **Cultural shifts during leadership transitions:** A new leader may change company culture or operations. Establish clear communication channels and support during the adjustment period to avoid disruption.
- **Resistance to change:** Employees, clients, or stakeholders may resist the transition due to uncertainty or fear of disruption. Clear communication and reassurance, alongside visible support from the outgoing leader, can ease this resistance.
- **Economic uncertainty:** External factors, such as market downturns or industry changes, can affect succession timing and execution. Building flexibility into your plan allows you to adapt as needed.
- **Inadequate planning timeline:** Rushing succession planning can result in oversights, such as missing opportunities for tax relief or failing to prepare the successor adequately. Starting early provides time to address these challenges methodically.
- **Balancing immediate needs with long-term goals:** Business owners often focus on short-term operational demands at the expense of long-term planning. Delegating daily responsibilities to trusted team members can free up time to focus on succession.

THE COST OF DELAYING SUCCESSION PLANNING

Delaying succession planning can have serious consequences. The FSB reports that many businesses without a plan face closure after the owner's departure, putting employees' livelihoods at risk.

Additionally, unplanned transitions can lead to disputes among family members, client loss, and a drop in business value.

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HOW WE CAN HELP

We understand that business succession planning can feel daunting. That's why we're here to guide you through the process, offering tailored advice considering your goals and circumstances.

Whether you're just starting to think about succession planning or need help refining an existing plan, we're ready to help. Our team can assist with valuations, tax planning, legal considerations, and transition strategies to ensure your business's future success.

Let's secure your business's future together – with expert accounting advice to guide every step.

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