

Step up

By Chris Ryan

your succession efforts ... even if you have no plans to step down

Preparing your brokerage for the next generation





It's something most of us prefer not to discuss or think about: the D-dash-dash-dash word. The great gig in the sky. The soil slumber. That "farm in the country" where we tell the kids the family dog went to live.

Unless you run a funeral home, death is not a pleasant business.

And because most of us prefer not to discuss or think about it, we also tend to procrastinate planning for it — or avoid it completely. As a business owner, that kind of non-strategy can be disastrous.

It's about legacy, liquidity and letting go ...

By their demographics alone, those in the real estate business — brokers, owners and managers especially — have good reason to give serious thought to begin creating a succession plan.

According to the National Association of REALTORS® 2008 Member Profile, 59% of brokers who do not sell are older than 55. Brokers who do sell skew slightly lower: 53% are older than 55. Among managers, 39% (of those who sell) and 44% (of those who don't sell) are older than 55.

"I just turned 70 years old, my other partner is 75, and our younger partner is 61," says Earl Shuttleworth, CRB, GRI, partner and broker at The Wine Country Group, an office of Frank Howard Allen REALTORS® in Sonoma Valley, Calif. "We have identified some candidates to succeed us that are evolving but no one has been selected yet."

Often, lack of a succession strategy comes from not fully understanding what succession planning is — and is not.

"Succession planning is not about selling your business," says John Reddish, president and founder of Advent Management International, Ltd., a management consulting firm based in Drexel Hill, Pa., and a succession expert. "It's having some understanding of the importance of who and what comes next and how to use that understanding to protect yourself. It's risk management, it's wisdom, and it's recognizing that 'I may not want to do this forever.'"

In his 30-plus-year career, Reddish, who writes a succession planning blog (www.thesuccessionplanner.com), has worked with all kinds of firms, including many real estate brokerages.

"One of the first questions I ask a CEO is, 'What happens to your business if you walk in front of a truck?' They think I'm crazy, and then they start thinking," he says. "When you lose a key owner, there's turmoil no matter what. Without having any plan, you begin planning in panic mode. We all saw what happened with Hurricane Katrina."

That's exactly the kind of debacle brokers like Shuttleworth hope to avoid as they contemplate their next steps in life.

"That's the reason we would like to identify candidates if any of those unexpected events arises," he says. "We're all vulnerable to those possibilities. The purpose of lining up candidates is for emergency succession and permanent succession on a timeline that everyone agrees on."

Should you walk in front of that truck, at a bare minimum, Reddish says, you should have somebody in place — your lawyer, accountant, consultant or some other trusted person — who can tell your employees and stakeholders what the plan is. Often, that plan is identifying the people who have the will and the talent to take over on short notice for the short term.

If no current employee fits the bill for that sudden event, he has recommended his clients create a list of five people in the industry that he could approach to stem the tide and keep the company afloat should something happen to the owner.

"The first issue is protection; get it in place," he says. "In the short-term, who do we call to make sure we have some interim management? Long-term, we can do some of that through insurance, and a lot can be prepared for on a risk-management basis."

"The business owner may not be ready to let go, but must be thinking about these things — even us boomers who thought we were going to live forever, flying around in a blue suit and cape," he continues.

Letting go, Reddish says, can be as simple as saying, "Within six months, I want to be out on my boat at least three months a year." But there's often a catch.

"I have to tell them, 'If you're responsible for 40% of sales, you're not going anywhere but on day trips until we can replace you,'" he says. "Whether it's risk or lifestyle, you have to prepare them, so that when the time comes, they're ready to hear the words. A lot of people think of succession as surrender. It's not. It just frees you up."

In Shuttleworth's case, one of his business partners wants to retire completely, while he is interested in continuing on for the next few years. They are searching both internally and externally for the right candidates for both scenarios.

“There are two issues: management and ownership,” Shuttleworth says. “And they don’t necessarily link. We’ve been talking to some of our career agents who have the resources to gauge interest in owning a piece of the company and using that as a retention device. We’ve had very positive reception to that idea.”

The Three Ls: Legacy, Liquidity and Letting Go

For brokers, owners and managers, succession planning comes down to a few important considerations, according to Reddish.

“It’s about legacy, liquidity and letting go,” he says. “Everybody in the business wants to be remembered for something. Sometimes in a sale, you can influence that.” Reddish recounts how he once sold a company after helping build it to where the owners could sell for the right price, only to see

“If they have a desire to leave at a certain point or cut back or want to bring a family member or junior partner along, timing and personal goals are important,” he says. For example, if a broker sees themselves losing their love for the business, they should leave sooner than later because that attitude will likely impact the business negatively.

So when to let go?

“Obviously, this is not a good time for real estate brokers to sell their companies,” Shuttleworth says, laughing. “2005 was probably the height of it. When companies are acquired, it’s for the profit they can throw off.” He is proud to say that though The Wine Country Group closed 2008 with a modest profit, he would like to see more of one before he decides to get out.

“We are confident we can build that back to where it was in the near term in the next two or three years,”



I’ve been in the business for 48 years, but I’m not ready to stop yet. As long as I can be an effective leader, I want to continue.

— Earl Shuttleworth, CRB, GRI

them take a deal from someone who was offering substantially less than another bidder.

“I jokingly say to CEOs sometimes, ‘Do you want to sell this business or have it adopted by a good family?’” he says. All kidding aside, the question is a legitimate one: How do you protect your lifestyle and get what you need out of the business when you need it?

The short answer, according to Reddish, is that you’ll probably have to work through a predetermined transition period. The good news, he says, is that very few of those bridge relationships go full term, allowing the seller to leave early, if he or she so desires.

he says. Beyond legacy and liquidity, perhaps the hardest “L” of all is letting go.

“I’ve been in the business for 48 years, but I’m not ready to stop yet,” Shuttleworth says. “As long as I can be an effective leader, I want to continue. At some point, I have to give up. I don’t want to be here if I’m not able to be productive.” And that’s the point, Reddish says.

“If you’ve been in your own business for a long time, it’s a challenge to leave,” he says. “I work with boomers. I’m a boomer. We’ve been in charge of a lot of the world for a lot of years. It’s a real challenge to the family and the successors.”

On one of his first succession engagements, Reddish

You can fill gaps no matter when you start succession planning ...

worked with a company where the family members in charge had hired some aggressive young people to come in and take over the business. Reddish was brought in to expedite the process because the family members just couldn't bring themselves to recognize that it was time and were delaying the transition. The deal fell apart.

"If you keep lingering because you're not ready psychologically, you won't be able to hold on to your successors," he says.

To pre-emptively work around that issue, Reddish sometimes takes what he calls an annuity approach. Working with the owner(s), he puts together a strategy to bring in a new management team with an option for the owner to transition out in five to seven years. At the same time, they execute a plan to harvest equity so that the current owner could maintain his lifestyle and leave on his own terms.

"What it gives us is the ability to meet my client's financial legacy and 'letting go' issues in a way that worked for him," he explains. "This method pays dividends immediately and down the line. It's becoming a more formalized and more accepted process."

If, like a lot of people, you have not even begun to plan, though, Reddish offers a familiar piece of advice from the financial planning industry: It's never too late to start.

"You can fill gaps no matter when you start succession planning," he says, disagreeing with the financial planners on one big point: Conventional wisdom says that most people need to replace 80% to 90% of their salary to maintain their current lifestyle.

"When you factor in the five points of wealth — 1. continuing to work; 2. Social Security and government plans such as Medicare; 3. investments and retirement funds; 4; and harder assets such as your home, collectibles, etc. — 5. you also have a business," he says. "You can usually do it for a lot less than the financial people would tell you."

He puts the number closer to about 60%, depending on how lavish your lifestyle and how much you want to travel.

"When you look at it that way, things get a little brighter," he says. "It becomes a more positive experience, and gives you the encouragement to get started."

Family meeting!

In many small businesses, real estate brokerages especially, family considerations play a vital role in succession planning. Ironically, some family-run businesses can be lulled into letting their guard down thinking they're more secure because the family is there should something go wrong. Hopefully, that's true.

Often, it's not.

Nine out of 10 of the 21 million businesses in the United States are family-owned, according to the Small Business Administration. Why is it, then, that only 30% of those companies succeed into the next generation, and even fewer — 15% — succeed into a third?

The first thing a broker or owner in this situation should consider is that if he or she started the business when the kids were young, their now-adult children might harbor some resentment toward the business itself.

"Many entrepreneurs think, 'I'm doing this so that my family's life will be better,'" Reddish says. "However, the family often looks at it as, 'We've been abandoned because of this dumb business.'" Then, when it comes time to implement a succession strategy, these same family members either don't want the business or try to sabotage it because of the wrongs they perceive it did to them — which quickly becomes destructive.

Conversely, if the business was already well-established when the kids were young, they might make better candidates because they see the business in a more positive light. In these scenarios, Reddish recommends that owners insist these family members take jobs outside of the family business or in a different industry altogether for a few years so that they have a better perspective when it comes time to consider taking on the challenge of running this family business.



If the second generation doesn't love it, they shouldn't be there ...

John Reddish

"I've seen too many family businesses where in the second generation, the children see it more as a piggy bank than as something they love to do, in real estate especially," Reddish says. "If the second generation doesn't love it, they shouldn't be there."

An unfortunate reality, though, is that most parents love their family and the family business.

"I tell them, 'Sooner or later, if you want to protect the business, you can. If you want to protect your family, you can — but you can't protect both!,'" he says. But if a business has weathered a first and second generation, it's usually humming along with some stability by the third.

"Growth only happens when you have profitability," he says. "By that third generation, you may have some family members who are interested and others who aren't. You need to have a way to separate those participating from those who are not." He cites oil baron John D. Rockefeller's family as an example.

"By the fourth or fifth generation, everyone wanted money," he says. "It was, 'Pay us and we'll go away.'"

To separate the non-active or disinterested family members from the more active or interested ones, one solution is to annuitize or pay out to the non-active ones before a confrontation flares.

"If a succession issue occurs at the time the will is read, there might be a fight over what the business is worth, who gets what and how it's distributed," Reddish says. Addressing this challenge early on can take a lot of the personal animosity out of delicate family struggles.

Shuttleworth doesn't have to worry about family issues as he and his partners mull their succession options.

"We've known each other for a century," he says, laughing. "You can't choose your family, but you can choose your partners."

Be De-selective

When looking at succession, legacy is an important ingredient, and finding the right person or people to take over can be more art than science. Sometimes, it's more a matter of de-selecting potential successors than selecting them, Reddish says.

People who have spent an entire career building this or-



It's about being able to sell when you want to for the price and terms that meet your goals.

ganization with their name on the door must think of what they would like to see happen when they are gone or no longer active. They must also consider the economic equation.

“The person willing to pay you the most may not run the business the way you want them to,” he says. “What’s more important: continuity or becoming a larger business where the franchise is a general service offering? You have to look at those cultural items.

“Who’s going to give me what I want: Is it the guy down the street who I fight with and compete with? Is it Century 21?” he continues. “It boils down to what you want to accomplish.” When you work through the scenarios ahead of time, the space exists to be able to see who is and who isn’t a fit for what you want to see happen. If legacy isn’t as important to you, that question becomes much easier to answer.

For most, though it’s very important.

“Our oldest partner really wants to retire,” Shuttleworth says. “He wants ownership succession, but we’re not interested in selling to an institutional type of buyer.”

“If push comes to shove, that’s a really good reason to have a succession planning ability,” Reddish says. “When you get to a crisis, you’ve already thought

through some of the possibilities.” Having the right leadership is especially important in a real estate firm, according to Shuttleworth.

“The interesting thing is that your primary assets are independent contractors who go home every night — and you hope they come back the next day, which is different than, say, owning a hardware store,” he says. “Part of succession has to do with personality and skills in an environment where people want to stay.”

And it’s important for Shuttleworth to keep that edge as he and his partners consider their next step in life.

“Our next closest competitor does 50% of the business we do, and their next closest competitor does 50% of the business they do,” he says. “We are way ahead of the pack. We do that by being on the leading edge of technology and having the right people. We’re always trying to do things a little bit better.”

In the end, Reddish says, it’s not a matter of just selling. It’s about being able to sell when you want to for the price and terms that meet your goals.

“Succession planning isn’t surrender,” he says. “It’s not letting go — it’s knowing that if you want to, you can. ♦