MANAGEMENT SUCCESSION

FAMILY CASE STUDY

The Morgan Family: Has It All Together

Summary

Ted and Sally Morgan have owned and operated a small beef operation for the last 40 years. Due to increasing expenses, their cow-calf enterprise has not recently been very profitable. The lack of profit has prevented Ted and Sally from saving much money for retirement. The Morgans have three adult children, Joyce, Jim, and Jill, and want to figure out a way to pass the management of their business to the next generation and secure resources needed so they can retire.

Family Background

The Morgan Beef Operation

Ted and Sally Morgan have owned and operated a small beef operation for the last 40 years. The ranch consists of 200 beef cows, 40 acres of hay, and some pasture land. The Morgan's sell their calves through the local sale barn. Due to increasing expenses, the cow-calf enterprise has not been very profitable in recent years. The lack of profit has prevented Ted and Sally from saving much money for retirement.

Sally and the Children

Sally also owns another small business in their community. She does not take a salary, but simply uses money from the business to help pay family living expenses, as needed.

Sally and Ted raised three children. The children are grown and have families of their own. Their oldest daughter, Joyce, is married and has a son. Jim, the only son, is a single father. The youngest sibling, Jill, is married with two step sons.

The Next Generation

Joyce, her husband, and son live in a large city about 70 miles away from the farm.

Jim and his daughter live near the ranch. He works for Sally's business. Jim's managerial responsibilities have been increasing as Sally takes more time off.

Jill and her family live in a modular home located on the ranch property. Jill has a job in town and her husband, George, is the only full-time employee of the ranch. Currently, Ted manages the ranch, while George does most of the physical work. Part-time employees are hired, as needed, to help harvest the hay and care for the cows.

Succession Planning

The Morgans want to figure out a way to pass the management of their business to the next generation and secure the resources needed to ensure that they can retire.

Interpersonal Issues: Family Meeting

At the suggestion of a business advisor, Ted called the entire family together to discuss the future of the ranch. Ted and Sally wanted to express their desires and hear what everyone else was thinking about the future of the business. Everyone was encouraged to express their thoughts, but they also had to be open to everyone else's comments.

Interpersonal Issues: Sharing Thoughts on the Future

Ted expressed an interest in slowing down or even retiring.

Sally wanted to have more time to spend with Ted, so she is interested in selling her business.

Joyce said that she likes living in the city. She is not interested in participating in the operation of the ranch, but wants to be sure her parents have enough money to be comfortable in their retirement.

Jim is interested in taking over Sally's business.

Jill and her husband enjoy ranch life. They would like to take over the business; however, they would like to make several changes to the operation to make it more profitable. They are concerned about Ted's willingness to relinquish managerial control.

Interpersonal Issues: Selling the Café

During the meeting, Sally revealed that her café business is worth somewhere between 225 and 250 thousand dollars. Since she and Ted have little savings, she would like to sell the business outright. The family agreed that while it would be nice to keep Sally's business in the family, it must be sold to help fund Ted and Sally's retirement.

Jim realized that while he would like to take over the café, it was not realistic since he did not have the funds to buy it. He agreed to help Sally find a buyer for the business.

Interpersonal Issues: Managing the Business

The family also agreed that Jill and George were the best successors to manage the business, but the other children should still retain an ownership interest in it. They agreed that Ted and Sally should set up a plan that would gradually transfer ownership of the business to the siblings with the greatest share and the management of the business going to Jill and George.

Everyone agreed to meet every year to evaluate their progress and discuss future strategies.

Business Issues

Years ago, Ted and Sally developed a vision statement, mission statement, and goals for the business. They documented them and shared them with the family and business advisors. They have used these documents to guide their decision-making and strategic planning for nearly a decade. Because they had such success with formalizing their vision, mission, and goals, Ted and Sally also developed a constitution for the business after learning about it in a local seminar.

Ted keeps meticulous business records and uses them to create quarterly financial statements. These came in very handy when he and Sally met with a lawyer last year to create an estate plan. Ted and Sally both updated their wills and living wills. The attorney also suggested that incorporating the farm would allow Ted and Sally to sell or gift shares of the corporation to their children over time. He suggested a five-year plan to do this. Further, Ted could receive a fixed income for his operational and managerial responsibilities. He also recommended that Ted and Sally gift each of their children enough cash to help pay for a life insurance policy on Ted.

During the five-year transition, Ted gradually released managerial control of the business to George. Each year, Ted and Sally sold and gifted a portion of their shares in the farm corporation to Jill and George until they owned 60 percent of the business. The remaining shares were gifted to Joyce and Jim. As Ted transferred management of the business to George, some of Jill and George's suggestions for the business were implemented. These changes helped to improve the profitability of the ranch. Throughout the transition, Ted, Sally, Jill, and George conducted monthly family business meetings to evaluate how things were going and determine next steps.

Succession Planning Issues: Years 1 and 2

The result of Ted and Sally's meeting with their attorney was a documented five-year plan for transition of the ownership and management of the business. This plan was shared with everyone involved in the business so that everyone knew what to expect throughout the transition period.

In the first two years, George took over the day-to-day management of the ranch. In addition to his wages, he received a 500 dollar per month management fee. Ted maintained control of the finances and kept all the records for the corporation. In accordance with their estate plan, Ted and Sally gifted five percent of their shares in the farm corporation to each of the children. They sold an additional five percent of their shares to Jill and George in year two.

Succession Planning Issues: Year 3

In year three, George increased his managerial responsibilities and received an additional 250 dollars per month. Although Ted maintained control of the farm's finances and records, he began to share the information and decision-making with George. Ted and Sally each sold ten percent of their shares in the farm corporation to Jill. At Jill and George's suggestion, the farm purchased 10 dairy goats and the necessary milking equipment. The goat milk was sold to the local goat milk cooperative.

Succession Planning Issues: Years 4 and 5

In year four, George began keeping all the ranch's records with Ted providing oversight. George's management fee increased to 1,000 dollars per month with his salary remaining the same. The changes made to the business allowed it to continue being profitable. To make room for the purchase of 20 additional dairy goats, half of the beef cows were sold and needed adjustments were made to fencing for the goats. Jill began making cheese from the goat milk for family and friends. George thought the ranch could increase its profits by selling the cheese at roadside vegetable stands and at a local store owned by a friend of Sally. In accordance with the estate plan, Ted and Sally sold 15 percent of their stock in the farm corporation to Jill.

At the end of year five, the entire family gathered together for another Family Council meeting. They learned that Ted was able to retire and that George assumed all managerial responsibilities of the farm. Since selling her business, Sally was able to travel with Ted and play with the grandchildren.