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Kreischer Miller Family Business Survey

The Impending Perfect Storm Facing Family Businesses



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Introduction

Privately-held family businesses are the backbone of our economy. They represent at least half of all companies in the U.S., according to the Family Firm Institute's *Global Data Points*. But they are constantly facing changes in the economy, customer demands, government policies, and competition. Add to that the dynamic of managing family relationships, and life quickly becomes complicated for these entrepreneurs.

In 2010, the first of the Baby Boomers turned 65. At that time, our country was two years into the Great Recession and most family business owners were not even contemplating retirement; they were focused on keeping their companies afloat. Even though things have come a long way since then, with several good years of returns from Wall Street and what appears to be a stabilizing economy, the last five years have not been easy for family business owners. They have faced tough decisions, like whether to right-size the workforce to adjust for slowing customer demand and whether to sell the business or shut it down.

It's no wonder, then, that so many of the Boomer-aged owners of our family business clients are telling us, "I'm tired." After years of challenges, many senior generation owners are finally ready to exit their businesses. But how prepared are they, really?

The answer may surprise you. **According to Kreischer Miller's 2016 Family Business Survey, 62 percent of senior generation owners plan to transition their business within the next 10 years. Yet 65 percent do not have a clear retirement plan and just over half (51 percent) do not have a succession plan.** These are quite staggering statistics for a population that generally plans to transition the business to the family. With such a gap between desire and readiness, it is perhaps no wonder that only one in three family businesses successfully transition to the second generation.

This survey report was designed to provide insight into what is shaping up to be a **perfect storm**: the dual challenges of preserving the legacy of the family business and successfully managing the exit of the largest and most influential generation of our time. Our hope is that by acknowledging and facing this perfect storm head-on, you will have more certainty and clarity about how to ensure the longevity of the business you have put so much heart and effort into for generations to come.

Methodology

Survey questionnaires were distributed electronically to middle market family-owned business executives in the Greater Philadelphia region, including most of southeastern and central Pennsylvania, southern New Jersey, and northern Delaware.

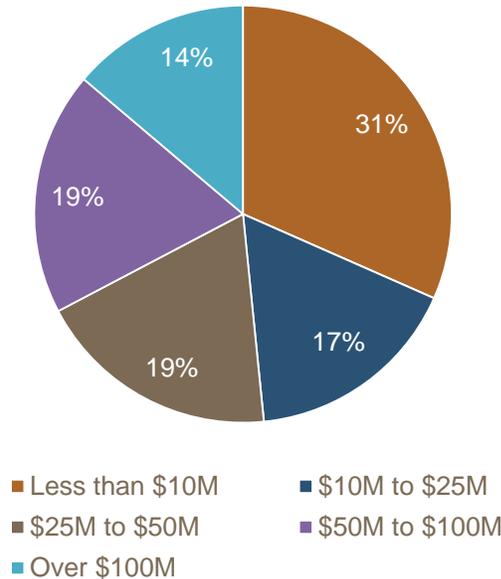
The survey was conducted online during a three-month period in 2015.



Source: WelcometoPhila.com

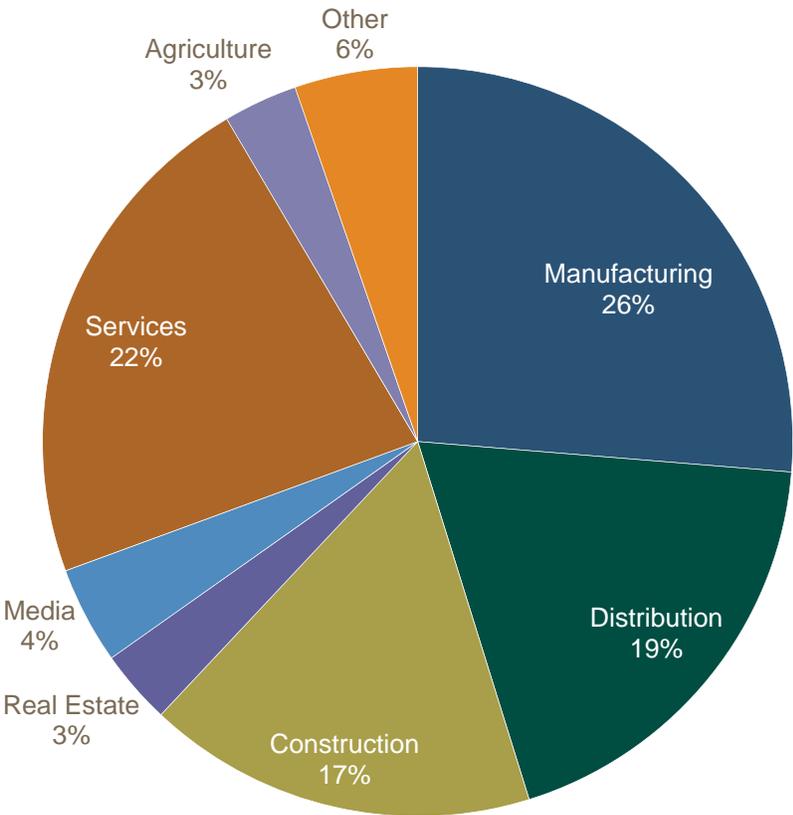
Survey respondents included only privately-held companies. Over one third of the respondents' companies (36 percent) have revenues between \$10 million and \$50 million.

Annual Revenues of Respondents



Methodology *Continued*

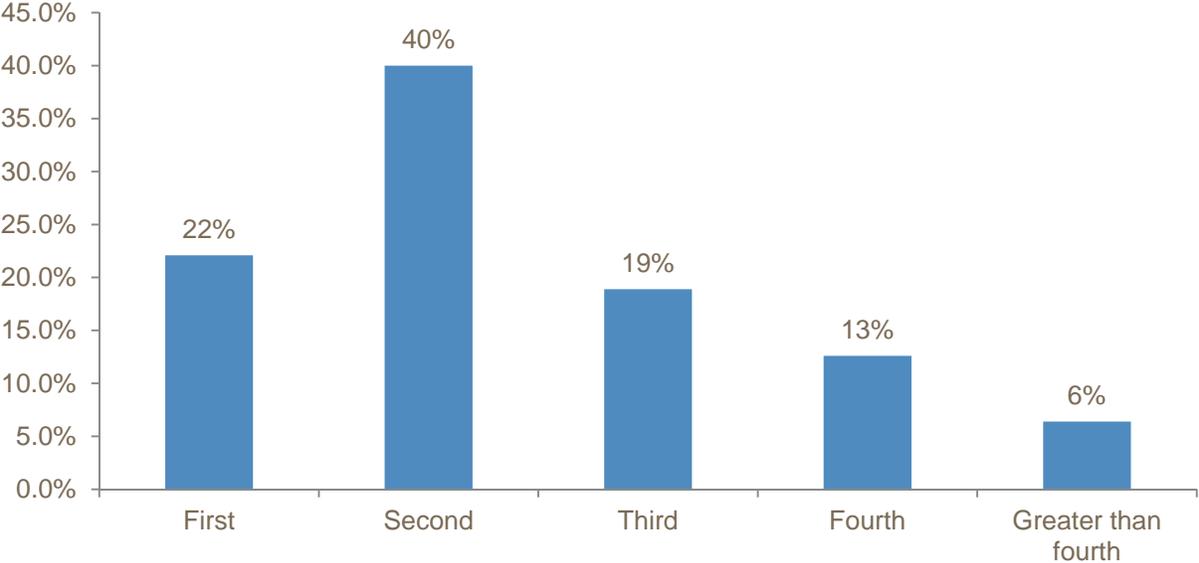
Respondents represented a diverse cross section of industries. The largest industry categories were manufacturing, service companies, distribution, and construction, which totaled 85 percent of all respondents.



Methodology *Continued*

Second generation businesses represented 40 percent of all respondents. First generation businesses accounted for 22 percent of respondents, while third generation businesses represented 19 percent. Perhaps unsurprisingly, a smaller percentage of respondents were from fourth generation businesses (13 percent) and fifth generation and beyond (6 percent).

Generation of Family Business

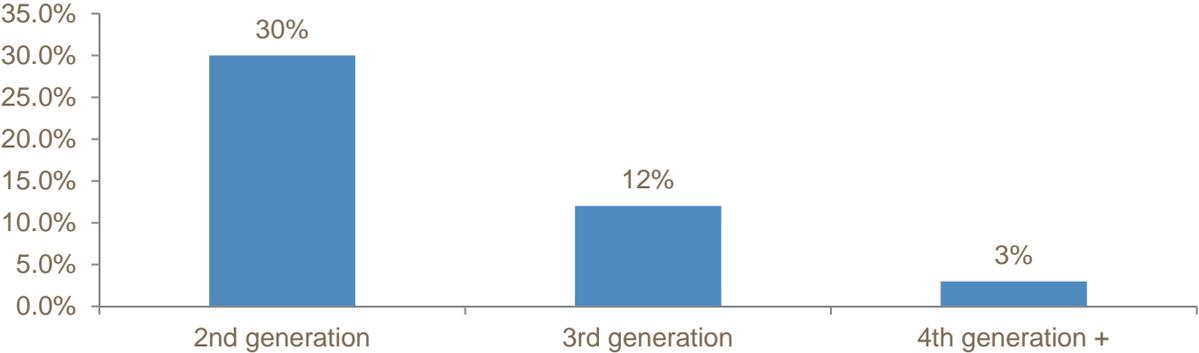


Leadership & Succession

Family businesses are under more pressure than ever. With over 6 million private businesses expected to change hands within the next ten years and the humbling statistics about the historic success rates of family business transitions, you can clearly see why.

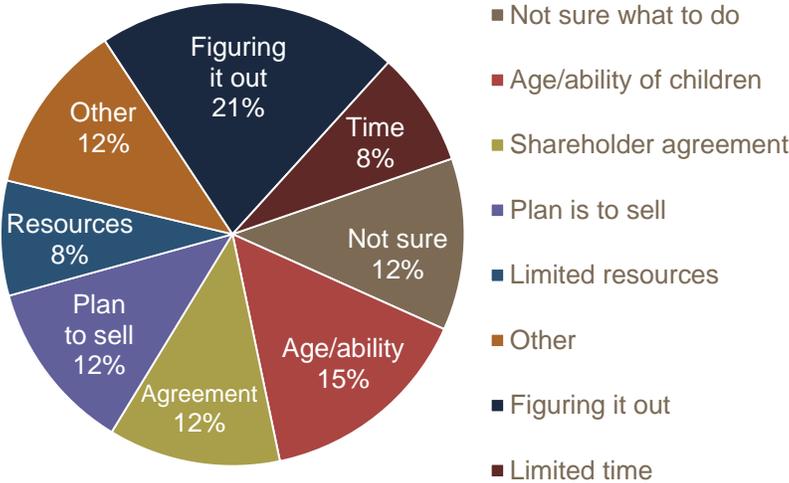
Family Business Transition Success Rate

Source: Family Business Institute, 2015



We asked participants whether they have identified the future leaders of their organizations and whether they have a management succession plan in place. Despite almost two-thirds (63 percent) indicating they have identified the next leader of their organizations, only 49 percent said they have a management succession plan in place. The top reason cited for not having a plan is that the business is still trying to figure things out (21 percent).

Succession Plan Obstacles

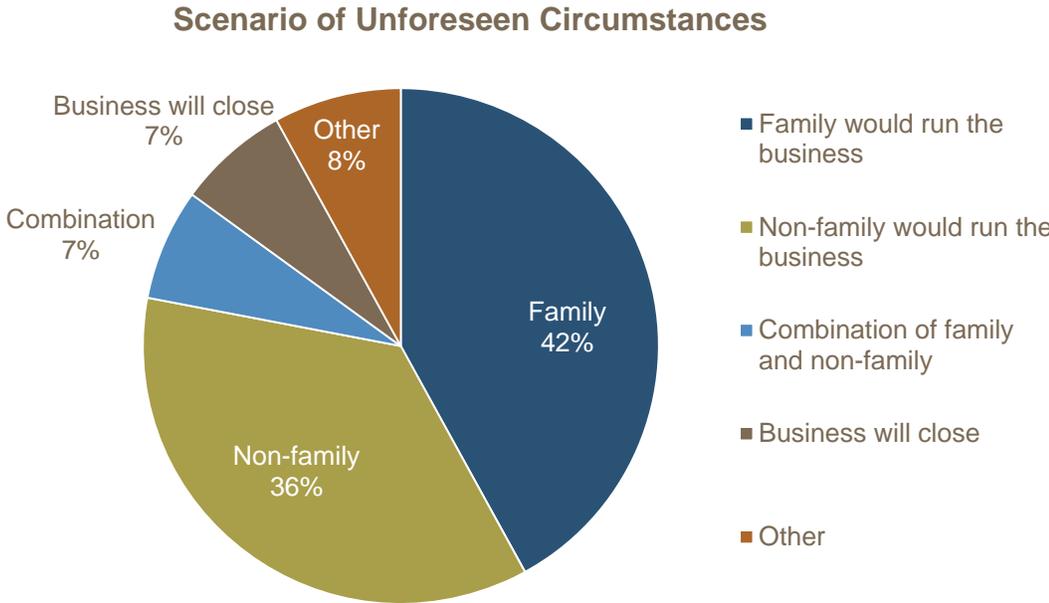


Leadership & Succession

Continued

We inquired whether participants have a written emergency plan that would take effect in the event of an unforeseen circumstance. Only 51 percent of respondents indicated they have a written emergency plan in place.

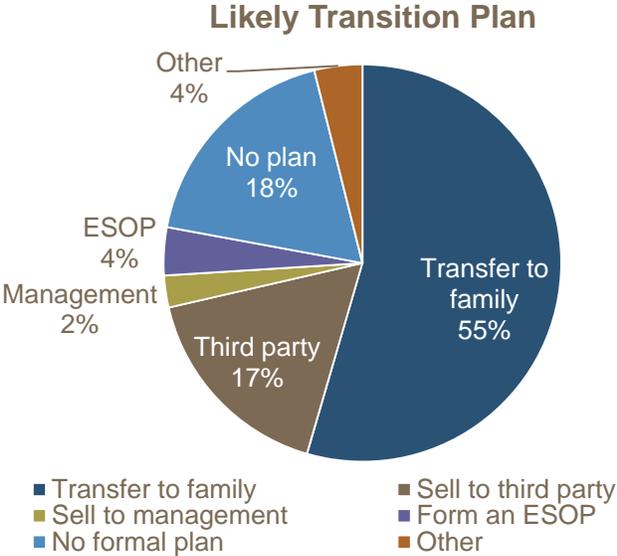
We also asked participants what they perceived to be the likely scenario or outcome should an unforeseen circumstance occur. The most common answers were that family members would step in and run the business (42 percent) or non-family managers would run the business (36 percent).



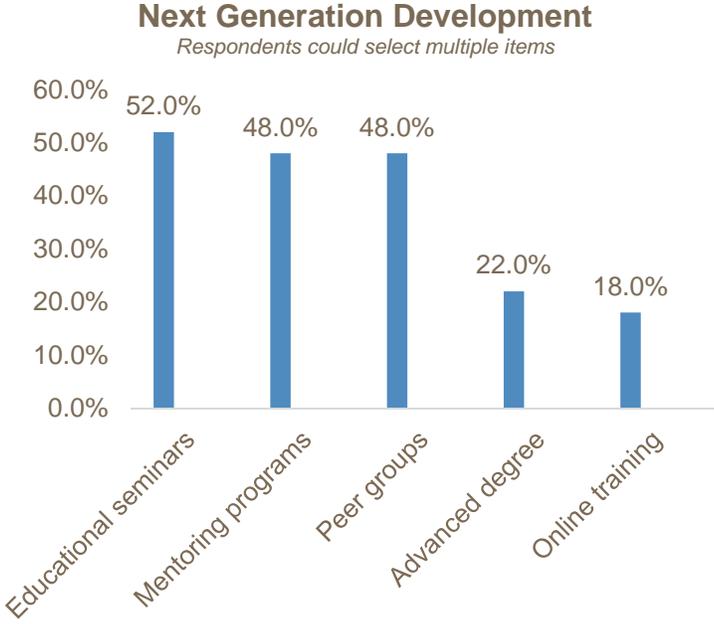
What is interesting is that the majority of respondents indicated that the family would step in and run the business in the event of an unforeseen circumstance. **However, that makes a large assumption that the family would, in fact, be ready, willing, and able to step in.** Given the historically low success rates for family business transition cited on the previous page, this is clearly a red flag.

Next Generation

When asked about the likely transition plan for the company, over half (55 percent) of respondents said they expect the business to transfer to family members. Other top responses included selling to a third party (17 percent) or currently having no transition plan in place (18 percent). Despite a large number of respondents expecting to transfer the business to family members, only 37 percent said they have a development plan in place for the next generation of leaders.



In businesses that have development activities in place for the next generation, educational seminars (52 percent), mentoring programs (48 percent), and peer groups (48 percent) topped the list. Other activities included paying for an advanced degree (22 percent) and online training (18 percent).



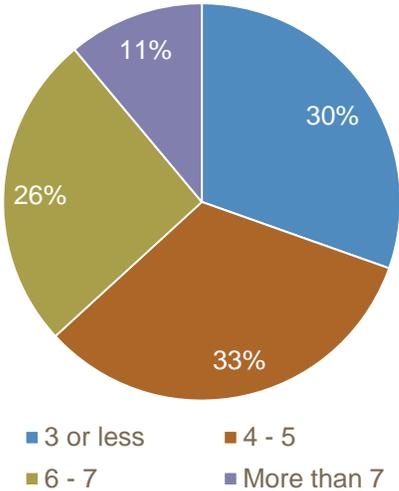
The message for the next generation: take your professional development into your own hands.

Governance

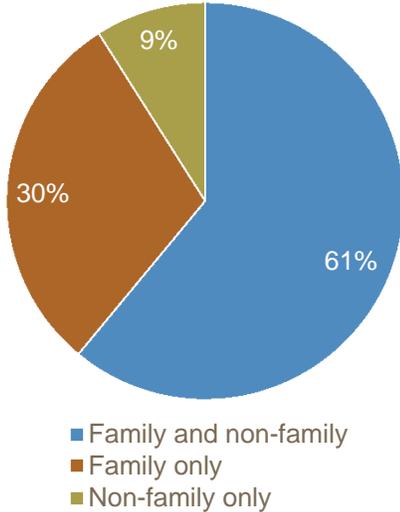
Slightly more than half of survey respondents (56 percent) indicated that they have a board; less than half (44 percent) do not.

The average board among respondents has less than seven members and is comprised of a mix of family members and non-family members (61 percent). About 30 percent of respondents have boards that are comprised of only family members, while 9 percent have non-family member only boards.

Number of Board Members



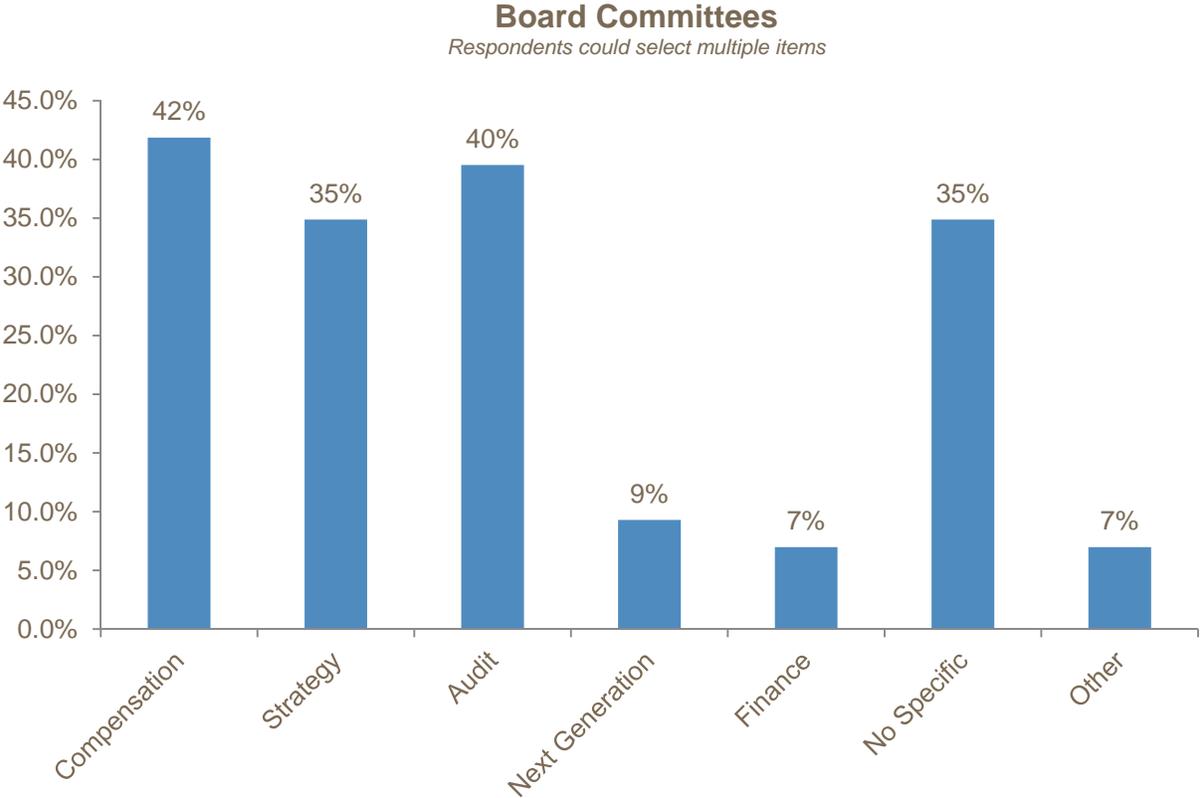
Board Member Composition



Most respondents indicated their boards meet on a quarterly basis (30 percent) or annually (26 percent). Interestingly, boards that are comprised of family members and non-family members tend to meet more frequently than family-only boards; 88 percent meet monthly, while 69 percent meet quarterly. Boards that only meet annually are predominantly either family members only (55 percent) or non-family members only (27 percent).

Governance *Continued*

The most common board committees cited by participants were compensation (42 percent), audit (40 percent), and strategy (35 percent). Thirty-five percent run boards without specific committees. Only 7 percent have committees for next generation leadership or finance.



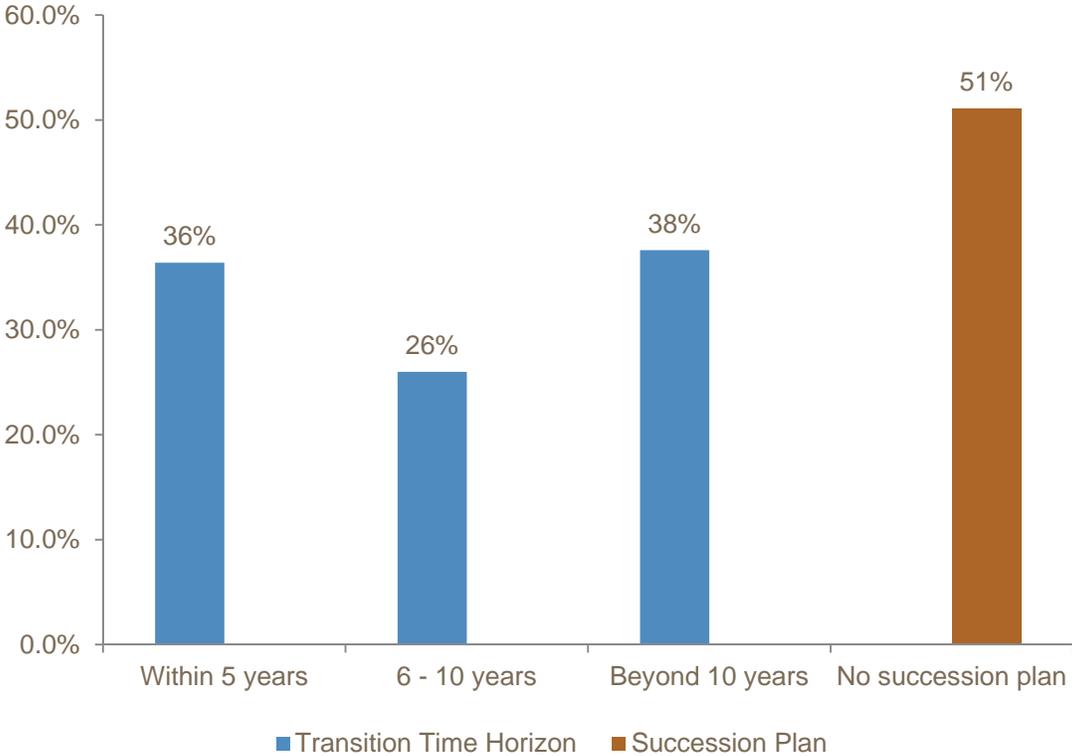
Even though more than half of survey respondents indicated their companies have boards, why have so few planned for succession?

Exit & Retirement

There was a fairly even split among the timeframes cited for the senior generation’s exit from the business. Thirty-six percent expect to leave within the next five years, while 26 percent are aiming for the next 6 to 10 years. Just over one-third (38 percent) do not expect to leave for at least 10 years.

Exiting the business successfully will be a challenge for the 51 percent of respondents who do not have a succession plan in place. And with 62 percent of senior generation owners saying they plan to transition out of their businesses within the next ten years, there is no time to waste.

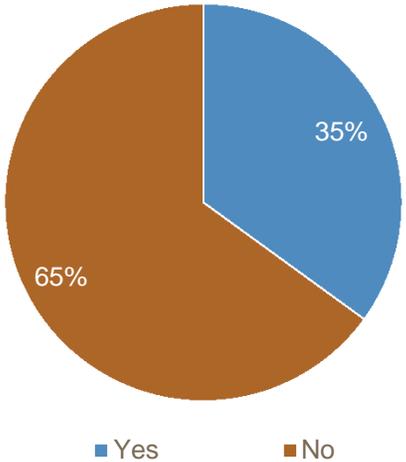
Transition Timeframe and Readiness



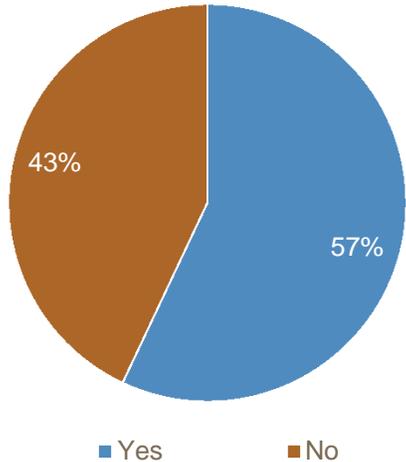
Exit & Retirement *Continued*

Another surprising finding involved the senior generation's plans for retirement. An overwhelming 65 percent of respondents said they do not have a clear retirement plan. Furthermore, when asked whether the senior generation has an estate plan that is clear to other family members as it relates to the business stock, little more than half (57 percent) indicated that such a plan exists.

Does the Senior Generation Have a Clear Retirement Plan?



Does the Senior Generation Have a Clear Estate Plan?

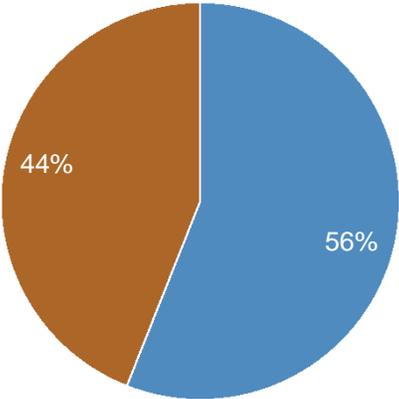


A gap clearly exists between the expected timeframe for the senior generation's retirement and the readiness of the business and the exiting generation.

Ownership & Compensation

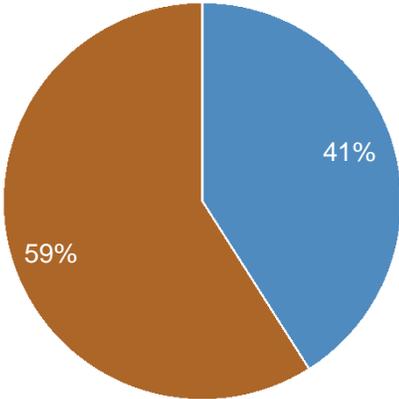
Survey results indicated that the majority of families (56 percent) believe family members should be required to work in the business in order to be given ownership. For families that allow family members to enter the business, slightly less than half (41 percent) require outside work experience beforehand. Generally, these businesses require at least three years of outside experience.

Should Family Members Be Required to Work in the Business to Be Given Ownership?



■ Yes ■ No

Should Family Members Be Required to Gain Outside Work Experience?



■ Yes ■ No

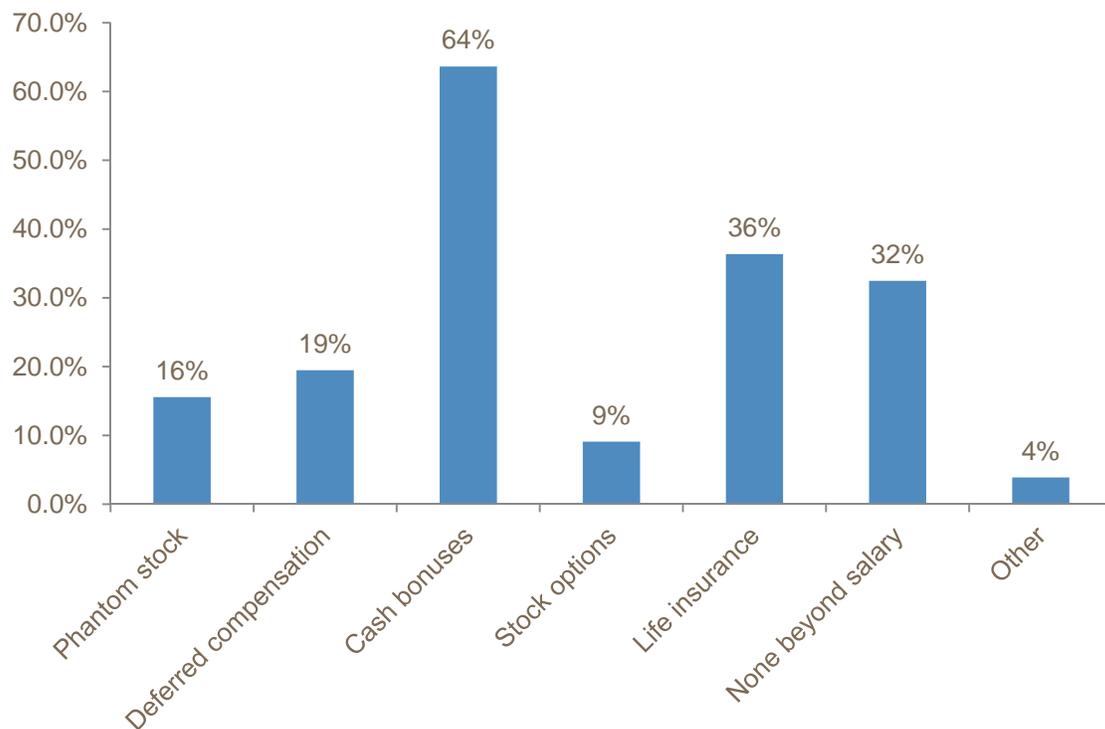
Ownership & Compensation

Continued

Owners often tell us their philosophy is that once you are a family business, you are always a family business. Most respondents (77 percent) do not allow non-family executives to have ownership in the family business. The most common method cited to compensate non-family executives in addition to salary was bonuses (64 percent).

Non-Family Executive Compensation

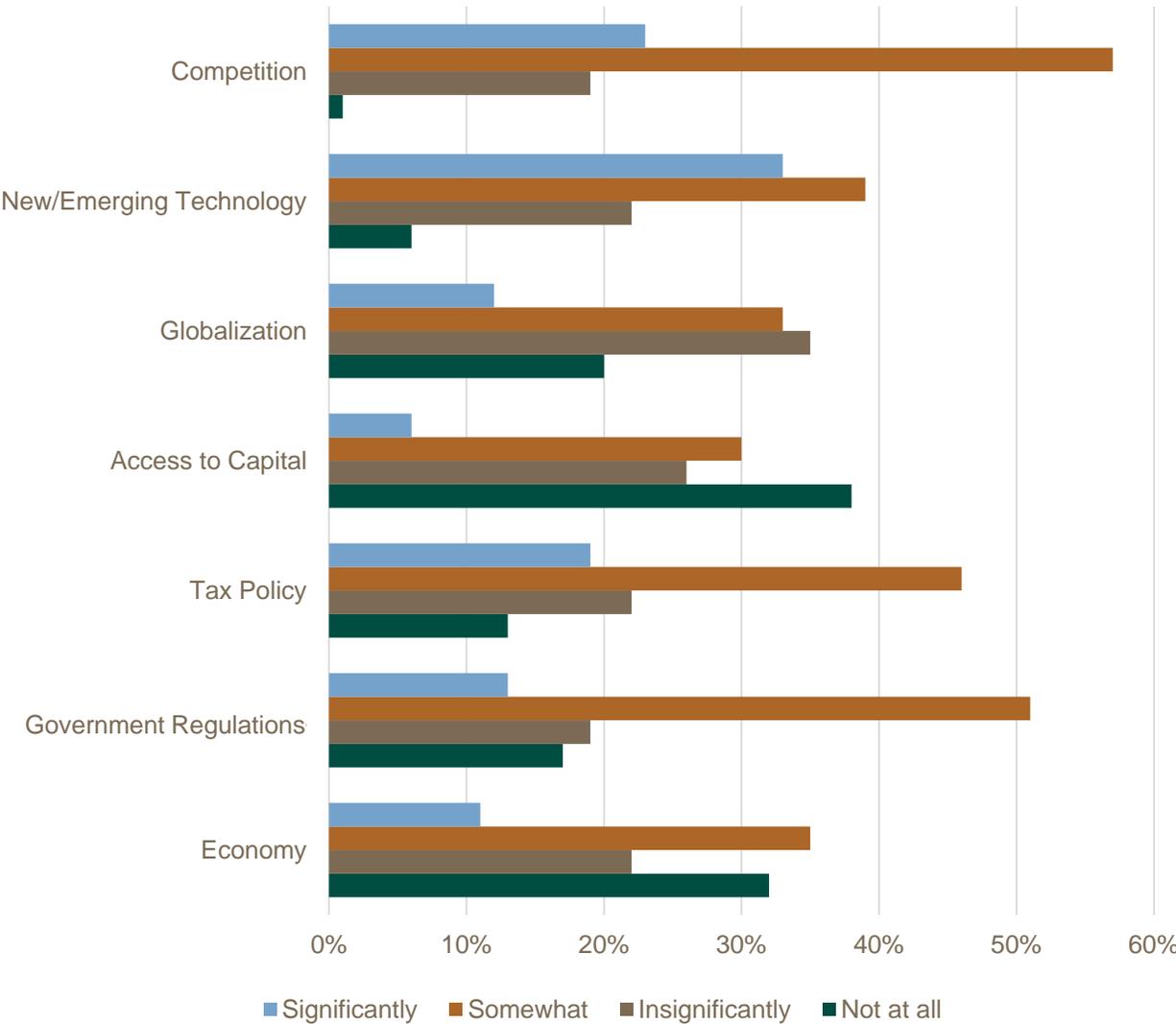
Respondents could select multiple items



External Factors & Future Outlook

When asked which external factors have impacted their businesses, the top areas cited by respondents were government and competitors.

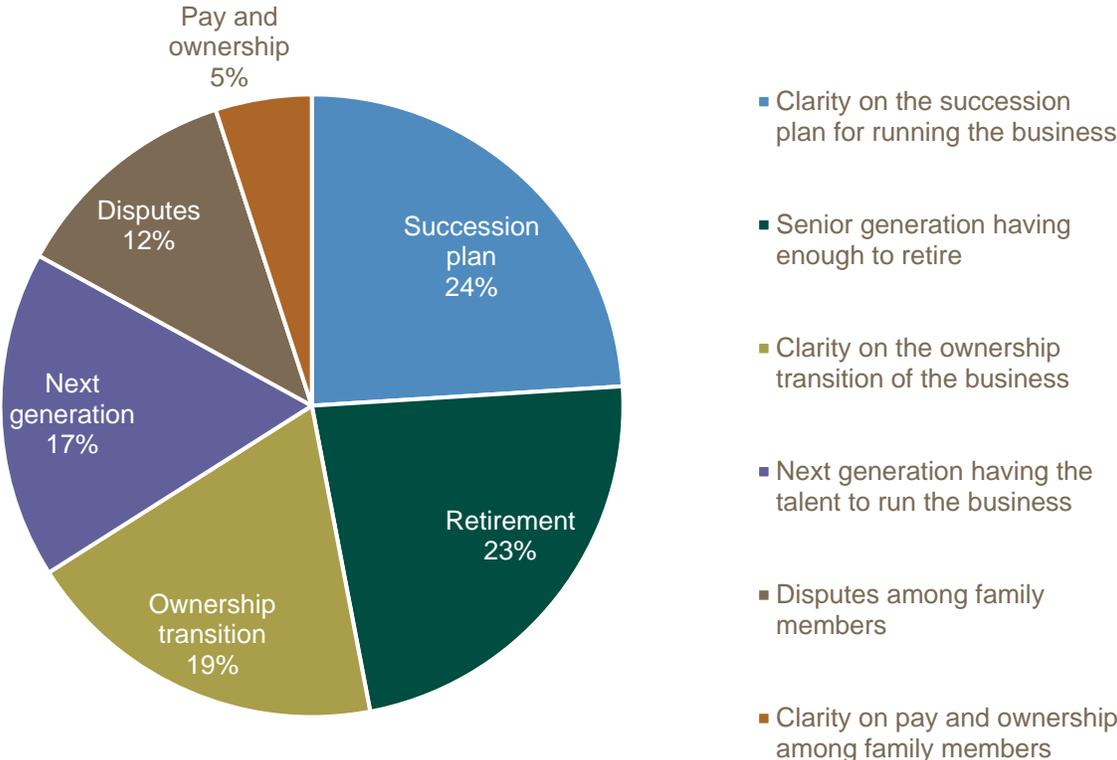
Impact of External Business Factors



External Factors & Future Outlook *Continued*

We also asked respondents to rank six key issues that commonly affect family businesses in order of importance. The top two issues – clarity on the succession plan and having enough money to retire – accounted for 47 percent.

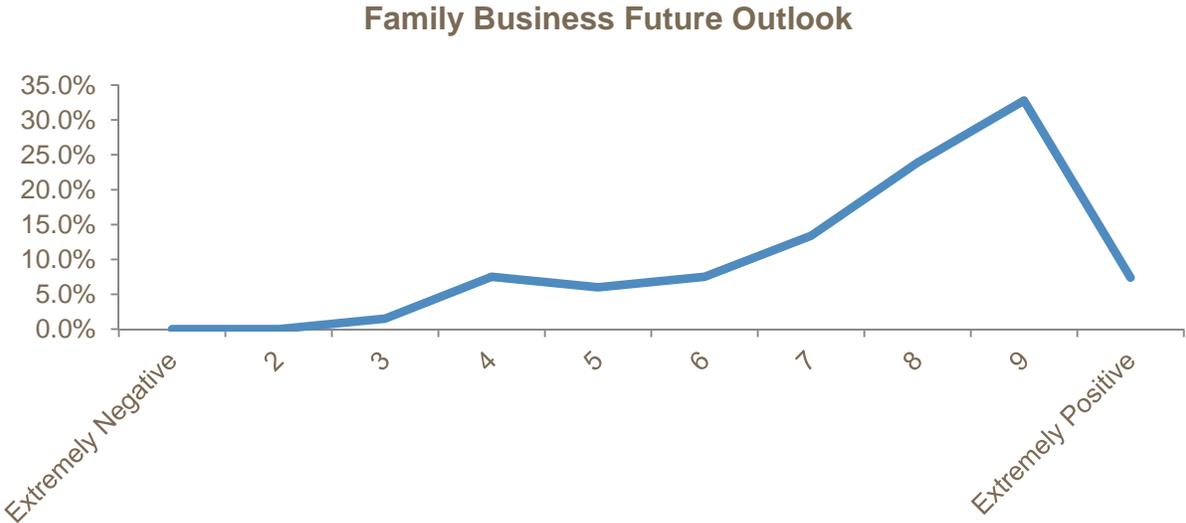
Issues Impacting Family Businesses



External Factors & Future Outlook *Continued*

Finally, we asked respondents about their outlook for the future. On a scale of 1 to 10, where 1 was extremely negative and 10 was extremely positive, the average score was 7.6.

The message: the future looks good!



About Kreischer Miller

Kreischer Miller is a leading independent accounting, tax, and advisory firm that has served the Greater Philadelphia area since 1975. We have built our firm to respond to the unique needs of private and family-owned companies, helping them smoothly transition through growth phases, business cycles, and ownership changes. The companies we work with quickly adapt and respond to changing market opportunities and challenges. That's why our focus is on being responsive, decisive, and forward-thinking. We're up to the challenge – always looking at the road ahead, not in the rear-view mirror.

Our people are leaders in accounting and passionate about helping companies achieve their goals.

Kreischer Miller's Center for Private Company Excellence

The Center for Private Company Excellence is a community – live and virtual – created by Kreischer Miller exclusively for private and family-owned companies. The first of its kind, the Center provides content, resources, tools, and information geared specifically toward the unique needs and issues of family and private companies, across the lifecycle of their organizations. It is also a forum for business owners and executives to interact and network with their peers as they address the challenges they face in improving their businesses.

Learn more at www.kmco.com.

For More Information

To learn more about the results of Kreischer Miller's 2016 Family Business Survey, or to discuss your company's needs, please contact your Kreischer Miller professional or the authors below.



Mario O. Vicari, CPA
Director, Kreischer Miller
Specialist, Center for Private Company Excellence

215.441.4600
mvicari@kmco.com



Steven E. Staugaitis, CPA
Director, Audit & Accounting, Kreischer Miller
Specialist, Center for Private Company Excellence

215.441.4600
sstaugaitis@kmco.com