encouraging successful business transfers

REPORT OF THE SEMINAR 7 JUNE 2005

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Encouraging successful business transfers: Report of the seminar 7 June 2005

Certified Accountants Educational Trust, London, 2005

Introduction

This report aims to provide a record of the main points that emerged from the joint ACCA/SBS seminar 'Encouraging successful business transfers' held on 7 June 2005. The seminar aimed to raise awareness of the challenges ahead to improve business succession rates.

THE ISSUE

In the UK, research shows that around 30% of closures might be viable businesses that close for lack of a suitable successor. Failure to plan effectively for the future not only affects the survival of the firm in question, but can also have serious implications for local employment and supply chains and, therefore, the local economy. Effective transfer of business ownership has the potential to drive productivity benefits through improved innovation, investment and skills.

There are a number of reasons why small businesses tend to be more at risk of succession failure. These include having owner-managers with a 'lifestyle' approach to business ownership and them placing less emphasis on succession planning. Against this background, more attention is being given to the provision of ownership succession advice by accountants and other business advisers.

There are important policy and research questions within current thinking and practice that need addressing before introducing new policies and initiatives. The aim of the seminar was to provide a forum to discuss these areas of need to know, and provide an opportunity for private and public sector to work together to identify the range of solutions to improve business succession rates.

THE DELEGATES

The seminar was attended by over 80 representatives from national government, English regional and devolved administrations, private sector specialists, key small business representative groups and a wide range of professional bodies.[1]

THE PROGRAMME

Chaired by Mark Gold, Partner, Silver Levene, the morning session focused on the evidence base for business transfers and specifically on research commissioned by SBS and ACCA respectively. The current data on business succession rates and the quality of the support and information available to small businesses were examined.

The afternoon session centred on eight working groups based on key issue questions, each chaired by a recognised expert. After discussion, the groups fed back their views to the other delegates. This was followed by a panel discussion.

[1] A full list of organisations represented is included in the Appendix.

THE WAY FORWARD

The key actions and issues raised in the afternoon workshop discussion were particularly valuable. The outputs will feed into the work of the Business Transfer Steering Group, chaired by SBS, as it develops and implements its detailed action plans. Not all proposed actions can be taken forward simultaneously, and a key role of the Steering Group will be to agree priorities. Within that context, initial emphasis is likely to be on the following action areas.

- A broad, awareness-raising campaign, initially aimed at intermediary organisations from both the public and private sector.

- A clearer definition of how the Business Link brokerage model can engage more effectively and consistently with private sector specialist advice and help on business transfer.

- Improved understanding, through focused research, on specific aspects such as the market for buyers and sellers, and valuation of intangible assets.

- The creation of a business transfer ‘toolkit’, to be available to all intermediaries, in both the public and private sectors.

- To ensure that all options for business succession, including more complex options such as employee ownership, are understood and available on a ‘level playing field’ basis.

- To learn from, and build upon, the significant work done on family business succession, in this broader context.

Summary of the presentations

This summary outlines the key issues raised in each of the presentations. Full copies of the slides can be accessed at www.accaglobal.com/smallbusiness.

MARTIN WYN GRIFFITH, CHIEF EXECUTIVE, SMALL BUSINESS SERVICE

Martin Wyn Griffith focused on the policy objectives of government.

- Small businesses account for over 99% of the UK's 4 million enterprises.
- SMEs account for 56% of employment and 52% of total UK turnover.
- Business transfer is an issue high on the Government's agenda. It is a significant element of government policy to increase productivity and GDP.
- The aim is to increase the numbers of successful business transfers where they make a positive contribution to the productivity and/or sustainable employment agendas.
- However, a certain level of business closure and 'churn' is one characteristic of a healthy, dynamic economy – sectors with a high number of business failures may be declining or no longer competitive.
- Successful business transfer can stimulate innovation.
- This seminar is a starting point to raise awareness, and the profile of this issue, among a wide variety of intermediary organisations.

PROFESSOR ROBERT BLACKBURN, DIRECTOR, SMALL BUSINESS RESEARCH CENTRE, KINGSTON UNIVERSITY

Professor Robert Blackburn provided an overview on the trends of business transfers.

- Business succession is becoming a pressing issue, partly because the number of small firms has increased, but particularly because of the rapid rise in business formation in 1970s and 1980s – these business owners are now in their 60s.
- There is a deficiency in the evidence base, with no single dataset on 'exits' and 'transfers', this problem needs to be addressed if sound policy decisions are to be made.
- Not all business closures are failures and evidence suggests that 'post transfer' businesses show better performance than new starts.
- From the seller's perspective business transfer fails because there can be a lack of 'exit' readiness by owners and a psychological difficulty with 'letting go'. Fee costs may also be a deterrent, together with difficulties in the valuation of businesses.
- From the buyer's perspective, business transfer fails because there can be a lack of awareness of what is for sale, difficulties in 'working out' what the business comprises and because people prefer to start their own business.
- Evidence suggests that there is a 'business transfer deficit' – the number of transfers is less than optimal and there is unrealised potential.
- There is a need to raise awareness of succession planning among business owner-managers above a 'need to know' issue and move from the reactive to proactive.

PROFESSOR IAN STONE, DURHAM UNIVERSITY

Ian Stone outlined the main findings from the SBS report *Passing the Baton: Encouraging Successful Business Transfers*.[2] The report is based on evidence from an international literature review, focus groups and consultation.

- One-third of UK SME owners have been identified as 'vulnerable' to age-related succession failure and this proportion is increasing. Best estimates suggest that 100,000 business closures every year in the UK are 'succession failures'.
- While not all business closures should be regarded as 'succession failures', for a number of reasons (not just those relating to age profile of owners), business succession is a growing market.
- Currently only 5–15% of family firms reach the third generation – an increasing proportion of business transfers occurs outside the family.
- The chances of business succession success is enhanced if the owner and successor have similar value systems, their relationship is based on mutual respect and trust and if the owner is prepared to 'let go'.
- Small firms tend to be more at risk of succession failure than large businesses as relatively few have a formal succession plan, they have fewer potential managers and often owner-managers have a 'lifestyle' approach to business ownership.

[2] Small Business Service (2004), *Passing the Baton: Encouraging Successful Business Transfers* (London).

DR CHRIS MARTIN, CHRIS MARTIN & ASSOCIATES

Dr Chris Martin provided an overview of the ACCA research *Accountancy Practices and the Provision of Ownership Succession Advice*.[3]

- Accountants have a very important role. Succession advice is not offered as a stand-alone service by accountants but embedded within accountant–client relationships and forms part of the wide provision of business and strategic advice.
- Succession advice involves combining expertise from individual specialist areas into packages of succession advice to individual client situations.
- Four main themes of advice provided by accountants are tax and ownership structure advice, valuation advice, business development advice and 'emotional' support.
- The succession advice most commonly provided relates to tax issues and often involves the structuring and timing of transactions in order to mitigate clients' inheritance, capital transfer and capital gains tax liabilities.
- The succession advice provided depends on the size of the business and the complexity of the succession processes involved – business closure is the natural exit route for the owners of many very small businesses.
- Clients' mindsets and attitudes towards exit and succession issues have an important bearing on how and when accountants provide succession advice.

[3] Martin, C. (2005), *Accountancy Practices and the Provision of Ownership Succession Advice*, ACCA Research Report No. 85 (London: CAET).

Eight group sessions discussed a variety of different issues before feeding back the key points to all delegates.

WHAT IS THE ROLE OF PUBLIC FUNDING AND ITS RELATIONSHIP WITH PRIVATE SECTOR SUPPORT – WHO SHOULD DO WHAT?

Chaired by Norman Watson, Wales Co-operative Centre.

- There is a need for some element of public funding to ensure information is available on the whole area so that awareness can be raised on this issue. There is also a requirement for public funding to support educational needs, to prepare individuals for business transfer, and for the development of a brokering/matching service for small businesses. The overall justification for public funding is that SMEs do not have the resources to fulfil these activities.

- As there is clear evidence of a market failure, there is a need for continued public subsidy to ensure deals do take place and transfers do occur. There is a need for the presence of an experienced and independent person/mediator who has credibility with both parties, who can ensure the deal is properly facilitated.

- Support for business transfers is fragmented, uneven and patchy. This is the case across England, Scotland, Ireland and Wales. Business transfers needs to be integrated into current services and policy development, this should be addressed as a fundamental public service issue.

HOW DO WE MAKE EMPLOYEE OWNERSHIP A MORE ACCESSIBLE BUSINESS TRANSFER OPTION?

Chaired by Patrick Burns, Job Ownership Ltd.

- The conclusion of the SBS report *Passing the Baton* was that employee ownership and buy-outs are highly viable options, but there is a massive lack of awareness of this issue among intermediaries, owners and employees which needs to be addressed.

- There needs to be a significant communications campaign which can be broken down into the following aspects.

  - Producing more straightforward, simple and clear guidance. There is need for more ‘how to’ knowledge so that individuals are aware of how to work through the succession process where the outcome is employee ownership in one form or another.

  - There is a need for careful targeting of advice. Accountants and owners were identified as the key channels, but government sources (eg Business Links) and trade associations are also very important.

  - Once the guidance is produced, there is a need to produce specific and sensible advice on how to obtain it. Good help and assistance is available, but individuals need to know where to access it. Good practice examples could be produced.

DOES THE TAXATION SYSTEM HELP OR HINDER BUSINESS TRANSFERS?

Chaired by Chas Roy-Chowdhury, Head of Taxation, ACCA.

- The UK tax system helps and does not hinder succession; indeed it is better than in other parts of the world.

- There is, however, a lack of clarity, certainty and consistency with the UK system. Small businesses require simplicity from a tax system. The key word is communication. Individuals are not fully aware of how the tax system works and do not know that they can actually avoid paying tax if they act at the right time and in the right way.

- Major barriers are a lack of awareness of the tax issues and existing, negative perceptions of complexity and expense. To improve the attraction of business transfer, significant effort must be put into raising awareness of the tax issues and of the costs likely to be incurred in handling them. Currently, much information exists, but it is not effectively communicated or disseminated.

- The group recommended that 'succinct' guidance of different aspects of the tax system (eg VAT, IHT) and how it impacts on businesses could be produced in a simple one-page format. This should be available through a variety of media – the group noted that there is perhaps an over-reliance on the Internet as a key dissemination vehicle.

- Suggestions from the Group included a development of alliances between different advisers eg accountants, solicitors and transfer agents, to encourage one-stop delivery of advice.

- Businesses should be encouraged to visit an accountancy firm from day one to develop a long-term relationship for on-going business advice, which would allow the opportunity for issues such as succession to be discussed. Accountants are professionals, qualified to give appropriate, high-quality advice. Additionally, this provides a quality control mechanism for the books and records of the business to be in order from the beginning and allows contact with a professional who will also provide succession planning advice.

IS ACCESS TO FINANCE AND VALUATION A BARRIER FACING BUSINESS TRANSFER?

Chaired by Stewart Dickey, British Bankers' Association.

- Overall, access to finance is not a real problem. However, there are problems with specific areas, eg funding an employee buy-out, with small businesses which do not have access to sophisticated funds and when valuing intangible assets.

- The problem is worse when the owner-manager wants to exit in a short timeframe and requires a cash price. Therefore, the funding process has to ensure management succession is in place. The timing is critical. Delayed consideration for the sale of a business can be a useful source of funds provided the vendor is prepared to take some risk and remain involved in the business.

- The valuation of fixed and real assets is not a significant problem. However, the valuation of intangible assets is problematic. There can be different views on value, especially between the seller and buyer and the bank as a lender. From a purchaser's and lender's point of view, once the owner has gone there is arguably no intellectual capital remaining in the business – it is a difficult area.

- The lack of knowledge of sources of finance can be a problem because of the variety available, eg business angels, venture capital, banks etc. It would be helpful for advisers and small firms to have a route map to take them to the kind of finance readily available. This not only helps vendors and purchasers find the appropriate finance, but will also serve as a reminder to owners to commence succession planning.

DO ETHNIC MINORITY GROUPS (EMGS) FACE ADDITIONAL BARRIERS TO BUSINESS TRANSFER?

Chaired by Professor Monder Ram, De Montfort University.

- The family and ethnic minority businesses (EMB) are synonymous. Business transfer for many first-generation businesses was less of an issue because there was a cultural expectation that the business would be transferred to their children.

- It is important to consider what the business is for. This has added resonance for EMGs. There are different motivations within first, second and third-generation businesses. First and second generation often had particular reasons, such as a desire get children into education. These reasons have an impact on business transfer. Failure was not seen as an option, the status of having a business was particularly important for many first-generation EMGs.

- The family can be regarded as a resource because of the strong family ties and an extended pool of potential successors to draw upon. It can also be a constraint, with a lack of willingness to take external advice and reluctance to bring in external management or lose some control/equity. Trust is very important. There can be gender problems in business transfer, at present almost all businesses are transferred between males. Women often play a strategic role in firms, but their contribution is not recognised.

- Strong family bonds represent a strength, but in Asian businesses this is now changing with the third-generation of family members being less willing to take on the business and many wishing to seek independent careers.

- Business advice is required when exiting a business; the advice is probably sector, rather than ethnic group specific. EMGs do not have much confidence in the expertise of public sector support providers (eg Business Links). The diversity of the different EMGs is important in intervention. If the adviser is from a similar background, the individual may be more receptive to advice.

HOW CAN WE ENHANCE THE QUALITY OF ADVICE GIVEN BY INTERMEDIARIES IN RELATION TO BUSINESS TRANSFER?

Chaired by Leigh Sear, Associate Director – Research, Wood Holmes Group Ltd.

- The quality of advice does need to be improved; a key issue is defining what actually constitutes an intermediary in the process of providing advice on business transfer, eg accountants, specialist business consultants, Business Links, chambers, banks, solicitors etc. There is a need for greater clarity in how the public sector engages with intermediaries in providing support, particularly in the context of the brokerage model, and the challenges and development needs of the intermediaries in working with the public sector.

- There is a need to learn from existing successful models of support where public and private sectors work together to enhance current and future relationships.

- There is little or no common understanding, data or tools across intermediaries in supporting business transfer, which leads to significant confusion and fragmentation, and sub-optimal support for the businesses in need.

- The proposal is to produce a ‘toolkit’ available to all intermediaries in both the public and private sector. Possible content would include:

  - a route map of the key intermediaries, who they are and what services they offer

  - a simple customer diagnostic tool, or at least access to an on-line diagnostic tool

  - a number of real business case studies describing the help and benefits that a business can receive

  - a clear statement of what the benefits are to the intermediary in engaging collaboratively with the business transfer agenda.

DO WOMEN FACE PARTICULAR BARRIERS TO BUSINESS TRANSFER?

Chaired by Erika Watson, Executive Director, Prowess Ltd.

- Women do face particular barriers to business transfer. However, the extent of the problem is difficult to quantify as there is no firm data and only anecdotal evidence. Research should be conducted on gender and ethnicity to identify any particular barriers to business transfer, whether they are perceived or real.

- There is a big issue of exclusion of women in family businesses. They are disappointingly likely to be passed over in succession even though they may have been effectively running the business.

- Women are also less likely to reach senior management positions so are less likely to be involved in management buy out’s. Government and business support organisations should identify case studies and role models for women to aspire to. There should be an awareness raising campaign to value women working in business.

- Women’s businesses are more likely to be lifestyle based, part-time micro businesses, in the service industry, and home based than are men’s businesses. Therefore measuring the ‘value’ of the businesses may make the transfer process more difficult.

- In terms of business advice, low expectations of both the owner and adviser can be an issue. Advisers can find it difficult to understand the business which results in problems in valuation. Exit planning should be part of the business from day one. The terminology used in business advice can be a problem and requires consideration.

WHAT ARE THE CONSTRAINTS/BARRIERS FACING FAMILY BUSINESSES? – SHOULD BUSINESS TRANSFER WITHIN THE FAMILY BE ENCOURAGED?

Chaired by Grant Gordon, Director General, Institute for Family Business (UK).

- There are a number of constraints/barriers facing family businesses, including the following.

  - Where a business has a strong ‘family ethos’, factors other than commercial profit maximisation may influence decision-making within the firm, therefore it may make different business decisions. In some cases, this might produce ‘social’ benefits but in other cases it could result in a firm failing to operate effectively and grow.

  - Small companies are prone to implosion where the group of shareholders fall out with each other, leading to destructive conflicts. Unless the family relationship is strong, the lack of distinction between the business and members’ personal lives can become a continuing threat.

- Firms which are entirely composed in management terms of family members may not have the same level of business skills and experience as other firms. This can be a particular constraint where family firms make a conscious decision to exclude or freeze out non-family members, either completely or from positions of influence within the firm, regardless of the contribution they might be able to make to the business.

- The family firm concept has much to commend it, in terms of providing employment opportunities and financial protection for family members. But it is not possible to argue that transfer within the family should be encouraged in each and every case. What is important is that, in the process of succession planning, there is a thorough assessment of the talents and aspirations of the next generation. If the next generation are interested in running the business and have the necessary skills and aptitude to do so, then transfer within the family might increase the chances of the business remaining viable.

- It is important to raise the level of awareness among family firm owners of the contribution which business intermediaries – primarily accountants and business support agencies – can make in terms of providing expert, impartial advice in the planning and execution of succession planning. It is, though, desirable for those intermediaries to acquire a greater understanding of the particular dynamics of the family firm in order to enhance the effectiveness of their services to the sector.

KEY POINTS FROM THE PANEL DISCUSSION

- There should be an increased focus on the downside of not making a succession plan. For example, paying out redundancy costs, a lease on premises which may be onerous and the major impact it can have on relationships.

- The terminology used is very important – an ‘exit strategy’ is suggested as an alternative to ‘business transfer’.

- Business transfer agents are reporting big problems with finding buyers. There are far more sellers on the market than buyers, a problem which needs to be addressed.

- This raises questions about making the market work – there could be a focus on encouraging individuals to take on existing businesses.

Summary by Professor Robert Blackburn

The seminar brought together a diverse range of experience on the issues surrounding business transfer and this stimulated the sharing of expertise and development of ideas. There was a great deal of rich discussion and we have a strong basis to move forward.

1. EVIDENCE BASE

The evidence base needs to be more authoritative and systematic, although it is clear that we have a lot of experience and anecdotal evidence. There is a need to clarify the agenda for further research.

2. OBJECTIVES

We have an aging labour force and business population and therefore need to do something to facilitate the process of business transfers.

3. COMMUNICATION

There is an issue of improving communication between buyers and sellers, intermediaries and the private and public sectors. Clearly there is an existing market place for buyers and sellers but this is underdeveloped and micro firms may require particular attention.

4. MARKET SEGMENTATION

There are many different needs as each business is so diverse. There is probably a need by intermediaries to understand that owner-managers view their businesses as unique.

5. ROUTE MAPS

There is need for clear route maps for those entering the business transfer market: as sellers or buyers. For example, there is one route for finding the appropriate business transfer agent and another for where to find help to fund the transfer process.

6. RELATIONSHIPS

There is a need to improve the relationships between intermediaries – banks, accountants, estate agents, solicitors, trade associations etc. All need to be brought on board to help businesses find the appropriate advice for buyers and sellers.

7. MARKET FAILURE

We must accept that there is a market failure here which needs to be dealt with. There are specific problems and issues for female business owners, employee buy-outs, micro businesses and EMGs. The problem of more sellers than buyers is very significant and was confirmed in the break-out workshops.

8. OWNER-MANAGERS

There needs to be a focus on owner-managers (the sellers) to understand their own emotional, financial and personal issues and objectives. They need to understand that they will face succession issues and this should be considered as part of an on-going process – not six months before the event.

9. THE BUYERS

The market needs stimulating to overcome prejudices about taking over a business – this already happens with franchising. Buyers need to give time to understand the needs of potential sellers. The methodologies for valuation need developing by intermediaries, particularly for intangible assets.

10. ROLE OF PUBLIC POLICY

There is a need to work through existing intermediaries used by businesses, for example accountants and trade associations. Public policy has a broad educational role in facilitating dialogue between agencies, generating the market for more buyers and a responsibility to stimulate more research.

Appendix

The following organisations were represented at the seminar:

ACCA
B & B Italia, London
Barclays Bank
Baxi Partnership Ltd
Black Country Business Link
Black Country Chamber & Business Link
British Bankers' Association
British Chambers of Commerce
Business Link for London
Business Link Solutions Ltd
Business Link Surrey
Business Link Tyne & Wear
Business Link Wessex
Business West
Cavendish Corporate Finance Limited
CBI
Centre for Enterprise
Comtek Network Systems Ltd
Co-operatives UK
Chris Martin & Associates
Davidson Consultancy
De Montfort University
Durham University
ECJ Associates Ltd
Enterprise Ireland
European Commission
Everywoman Limited
Great Western Enterprise
Greenwich School of Management
Harrow in Business
Highlands & Islands Enterprise
Hines Harvey Woods Ltd
HM Revenue & Customs
ICAEW
Ilyas Patel and Co.
Institute for Family Business (UK)
Job Ownership Ltd
Kingston University, SBRC
Lakey & Co National Business Agents
ME Harris
NatWest
National Black Women's Network (NBWN)
Newbond Accountants
One Northeast
Ownership Succession Ltd
Oxford Institute of International Finance
Pridie Brewster
Professional Contractors Group
Prowess Ltd
Scottish Executive
SEEDA
Selection Services
Silver Levene
Small Business Council
Small Business Service
Sowalfin S.A.
The Forum for Private Business
The International Centre for Families in Business
UCE
University of Brighton
Wales Co-operative Centre
Welsh Assembly Government
Wood Holmes Group Ltd