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## **Business Succession -**

Success factors and implementation recommendation in the event of a company succession

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#### Abstract

This article deals with the key factors of a successful company handover. The aim is to use a qualitative content analysis to determine which factors are relevant to this project. The research question is therefore: 'What are the success factors for a successful transfer of the company?'. This article relates to seven factors that are relevant to this. This issue is of great economic importance. It is a question of preparing the transfer of the company for the employees, the outgoing shareholders, the incoming shareholders, the coordination on the size and payment method of the purchase price, the drafting of contracts, the inheritance situation, and the preparation of a company concept with a timetable. Of course, in the end, implementation is also presented based on these factors.

Keywords: Succession, Inheritance Law, Shareholder Management, Contract Design

JEL codes: D00, D01, M20

## 1. Introduction

This article deals with the key factors of a successful company handover. The aim is to use a qualitative content analysis to determine which factors are relevant to this project. The research question is therefore: What are the success factors for a successful transfer of the company? This article relates to seven factors that are relevant to this. This issue is of great economic importance. It is a question of preparing the transfer of the company for the employees, the outgoing shareholders, the incoming shareholders, the coordination on the size and payment method of the purchase price, the drafting of contracts, the inheritance situation, and the preparation of a company concept with a timetable.

#### 2. Methods

The purpose of this article is to answer the following research question:

#### 'What are the Key Success Factors for a Business Succession?'

In answering this research question, attention will be paid to the following aspects of the current state of research on the subject:

In order to answer the proposed research question, an extensive literature research and a qualitative literature analysis were carried out.

For this purpose, the following databases/library catalogues were used for literature research:

- SpringerLink
- SCOPUS
- ISTOR
- ABS Academic Journal Quality Guide
- PRO-Quest
- EBSCO Host
- Google Scholar
- Google Search

The following search terms were used as part of a targeted literature search.:

- Unternehmernachfolge
- Strategien Unternehmernachfolge
- Nachfolgeregelung Unternehmen
- Nachfolgeregelung Unternehmensübergang
- Gründe Unternehmernachfolge Nachfolgeregelung
- Gründe Unternehmernachfolge Nachfolgeregelung Mittelstand
- Motivation Nachfolgeregelung Mittelstand Deutschland
- Unternehmensübergang Mittelstand Deutschland Gründe Strategien
- Unternehmernachfolge Gründe Strategien Mittelstand Deutschland

Literature research identified 365 potential sources, 155 of which were identified as relevant sources. All sources which met the generally valid scientific requirement of the level of detail and the quality of the preparation were considered relevant. Twenty-five primary sources were used in this work. These are all scientific publications and articles in scientific journals. These are mainly recent works with a release date of more than 2000. The oldest work of W. Freund 'Family Company Succession' dates back to the year 2000. The most recent work is by M. Schwartz 'Generation Change in The Middle Class' from 2018. Based on this research, the following topics are the leading factors for a business succession.

Preparing employees
Preparation of the outgoing shareholders
Preparation of the incoming shareholders
Vote on the scope and method of payment of the purchase price
-Purchase price payment in an amount
-Purchase price payment in instalments
Preparation of the necessary contracts
Inheritance situation
Creation of a business concept including schedule

Based on this, Implications will be shown in the conclusion part.

### 3. Results

The successful design of a succession not only involves the handover process as such, but with this design of the handover process, the foundations for a successful future of the company are also laid.

The preparatory work concerns the outgoing entrepreneur as well as his successor. This work requires time that an entrepreneur usually does not have. A competent consultant can provide very good services here. We would also like to point out that a succession – if it is to be successful for entrepreneurs and successors – cannot be done on the side [10].

In the following, a grid for entrepreneurs and for the successor is to be presented to prepare for a transfer of business.

#### 3.1. Preparing the employees

Changes affect people who, through uncertainty about what is to come and are expected of them, develop fears, and thus become a restraining factor.

Since the employees of a company are an underrated capital of the company, so far often, every owner who wants to leave his business and every successor who wants to take over a company must be clear that he can use this human capital, but also to raise it against himself. Forms of resistance that keep ongoing are "internal dismissals" and "service by regulation", little willingness to work overtime, statements such as "We have always done this, this is no different", but also open and secret intrigue. Employees at all levels of the hierarchy have a wide range of possibilities, actions, and behaviors at their disposal. This is a critical factor in the transfer of companies, which has so far received too little attention [2].

In addition to an open information policy towards employees, it is also advisable to carry out the development of strategies together with the employees or employee representatives. This creates trust among employees, promotes their motivation and possesses the charm of a first "to-be-together" of employees and new boss.

## 3.2. Preparation of the outgoing shareholders

An outgoing boss must also be prepared for his departure. Time and again, there are examples in which the entrepreneur who wants to leave is unable to let go of the reins. This results in attempts at interference that lead to conflicts and do not have a beneficial effect on the further development of the company [6].

Preparing for the exit includes, above all, a timetable that not only defines steps to exit from day-to-day business, but also regulates a transition of competences. This successive transfer of competence must be binding on the outgoing entrepreneur. If the outgoing entrepreneur sees or thinks to see gross errors of his successor, fixed rules can be agreed, e.g., the establishment of an advisory board or arbitral tribunal.

### 3.3. Preparation of the incoming shareholders

The successor also needs preparation and, in many cases, also an accompaniment during the takeover process:

The focus here is on

- -the development of clear post-transition objectives, familiar with the specifics of the company regarding
  - -Staff structure
  - -Organization of the company
  - -Weaknesses
  - -Products and their markets
  - -Manufacturing know-how, development, and business potentials
- -the review also of one's own abilities (e.g., decision-making, communication, leadership behavior).

In this case, too, the preparation is accompanied by an external coach, not only as a guide and know-how carrier, but also as a "mirror" during the handover phase [13].

An important tool for successful preparation is discussions between entrepreneurs, successors, managers, and employees, moderated by supervisors/consultants [15].

## 3.4. Vote on the scope and method of payment of the purchase price

As a rule, the purchase price will be on a scale even for medium-sized companies that a successor will not be able to easily pay for from its own resources. Therefore, there are useful ways to pay a purchase price:

- -in an amount
- -in instalments from the company's profit
- -in the long term as a body or time pension.

In any case, the purchase price must be paid

- -liquidity-friendly: the company's liquidity to maintain operational readiness is not jeopardized,
- -in a substantial way: it may not be paid out of the company's substance (e.g., by sale of operating assets) and
- *Profit-friendly:* payments may only be made from the pre-tax operating result and the operating result may not be negative because of these payments.

#### Purchase price payment in an amount

To pay a purchase price in an amount, the successor will often be dependent on accompanying bank financing.

In addition, the one-off payment of the successor creates an interest disadvantage compared to the purchase price payment in instalments. Even if the transferor is required to pay an interest on the instalments under a partial payment agreement, the transferor will often be able to agree on a more favorable interest rate than with his bank. On the

other hand, unlike the seller, the bank will place clear requirements on collateralization when financing a one-off payment [4].

#### Purchase price payment in instalments

Here, payments are made from the cash inflows received by the acquirer from the company. These cash inflows can be income, profit share, commission or other. Here too, however, this amount must first be generated from the company in such a way that the company's viability is not jeopardized by the deduction of funds [1].

The purchase price may be treated as a *loan* from the transferor to the successor, which is to be paid as planned by the successor from his income, etc.

In the case of an agreement on a *personal or temporary pension*, the present value of the pension must be determined, whereby the present value of a life annuity based on the death tables is again based on the purchase price and the present value of a temporary pension is based on the agreed time frame of the payment [5].

The payment of the purchase prices as a permanent *burden* has the advantage that value change clauses can be incorporated, which determine the monthly payments e.g., turnover, gross profit, or other quantities. In addition, this variant of payment of the purchase price creates a significant tax advantage.

Compensation may be payable if, instead of a sale of the undertaking, the undertaking is transferred to the successor by way of an anticipated succession and the latter provides benefits to the trader to compensate [9].

## 3.5. Preparation of the necessary contracts

Numerous contracts are affected by an entrepreneur succession. The most common contracts are to be concluded or adapted:

-Company purchase agreement

(called share transfer agreement; in particular, the following points should be reviewed

name, registered office, purpose of company, shares, voting ratios, mode for the managing director election)

-Managing Director's contract (rights, obligations, remuneration)

In addition, the following points need to be clarified in particular:

- -Protection of the successor to the tax office and social security (Certificate of safety from the tax office)
- -Declaration of exemption or bank guarantee of the entrepreneur in favor of the successor for

Deferred taxes

- -Dismissal of the entrepreneur from given collateral/guarantees
- -if applicable, pension agreement, if the purchase price is to be paid in partial payments
  - -if necessary, land register registration of such a pension obligation

- -Remuneration scheme for the entrepreneur for consultancy work
- -Customer care as well as acquisition of new customers
- -Agree on a non-compete obligation for the previous farmer
- -existing insurance contracts check for uncovered risks or double insurance: A comparison of contributions can also help to reduce costs.

#### 3.6. Inheritance situation

The BGB does not have a prescribed regulation for a successor. The HGB also does not provide for such regulation. It only permits the continuation of the company, provided that this is already provided for in the social contract. Similarly, there is no rule on how a company can be protected from access in the event of an inheritance if a succession is suddenly forced upon the death of the entrepreneur.

It therefore offers to conclude company contracts with the intended successor during his lifetime, provided that these contracts only become valid by means of the inheritance contract or the will. The social contract and the inheritance contract must, of course, be coordinated with each other and formulated without contradiction. This is to avoid protracted disputes to the detriment of the company. In the drafting of the contracts, mandatory part claims and compulsory part supplementary claims must be considered. Regulations to protect against excessive withdrawals and compensation payments to the departing heirs are intended to protect the company from financial overload. Similarly, claims of non-marital children must be considered [8].

From all this, the importance of an injunction arises because of death. This injunction must consider that in a community of heirs, the heirs are liable for all liabilities. If necessary, an executor of the will should be appointed at an early stage.

Finally, formal requirements for the various contracts must be observed to prevent incorrect or missing formal requirements from ineffectiveness in the wishes of the entrepreneur.

## 3.7. Creation of a business concept including schedule

A business concept is of great importance and includes a timetable. Some important and indispensable points of such a business concept are presented below.

Building on the vulnerability analysis, the company concept formulates the direction for the future regarding

- -Products, product lines, further development, quality
- -Markets and customer loyalty
- -Marketing and pricing policy
- -optimizing business and production processes
- -the development of personnel
- -the financial basis of the company (financing, liquidity etc.)
- -the business, investment, and financing plan

as a *target concept*. This target concept can be compared with the actual state from the vulnerability analysis. This comparison can be used to deduce deficits that serve as starting points for change [11].

These changes can be attributed to action steps, which must then be worked out in detail with the managers.

In addition to an open information policy towards employees, it is also advisable to carry out the development of strategies together with the employees or employee representatives. This creates trust among employees, promotes their motivation and possesses the charm of a first "to-be-together" of employees and new boss [14].

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# 4. Conclusion - The implementation of the transfer of the company

The implementation of the transition must be given as much attention and care as preparation. The following indications draw attention to the sensitive situation of a company during the transition phase.

In our article from April 2020, which was published in the International Journal of Management, Technology and Engineering, we have already pointed out the possible impact of international trade restrictions due to the cancellation of trade agreements and Brexit, as well as the beginning of the COVID-19 pandemic for the national and international economy. At a later stage, I plan to study and describe the effects of both problems in detail. SMEs seem to be better able to deal with trade restrictions and Brexit - because they are more predictable than with the Covid-19 pandemic [18].

The serious difference can be explained by the unforeseen, rapid emergence of the pandemic, with the most massive impact on the lives of the world's population and businesses, the perceived helpless strategy of governments, and the unforeseen and post-effects of the pandemic.

In this respect, the M+A sector, particularly for SMEs, has come to a sudden standstill from April 2020. As a result, much-needed company successions have not taken place and many will no longer take place, either because the companies have either become insolvent or cannot be transferred now due to the prospects. The following example may be an example [14].

The author spent two years accompanying an SME in the consumer goods sector on an M+A project. The company generates sales of approx.  $\in$  100 million and has excellent prospects for the future. The results of the past years have been excellent, and the company works with -0  $\in$  debt. Until March, several suitable candidates were available for the handover of the company. From April, negotiations were on the way, so that an interim solution had to be found before negotiations had to be reopened and an expected conclusion was reached [22].

The example illustrates the importance of timely and well-prepared company succession.

## 4.1. The psychological situation

Even if the successor comes from the company or the family, by moving up to the successor he becomes an unknown size at first. In addition, each successor meets established structures and a specific corporate culture. This applies to the managers, the employees, the customers, the suppliers and finally to the accompanying bank. The successor confronts this with his own leadership style [17].

A particular difficulty in this context is the letting go of the old owner. Here, both the outgoing entrepreneur and the successor will be able to agree on rules of the game

together before the transition is carried out. To take the new company to the parade and show him where to go also means making it clear to the workforce that the real boss is the outgoing entrepreneur. This has long-term significant disadvantages for the successor, who will have to fight against the entrepreneur first and after his departure for a long time against the shadow of his predecessor. In the worst case, it means the (premature) end for the new, possibly even for the whole company [11].

In such a situation, an experienced consultant/moderator should be called in, who can help to counteract such tendencies effectively.

#### 4.2. Model for the successful introduction of a successor

First, the *time perspective* of the transition must be considered. Before the introduction of the successor, it must be clarified between him and his predecessor how the transition is to take place. Differences were made between a gradual transition and a transition in one step.

As a rule, the employees must be informed at an early stage of the upcoming change. The outgoing entrepreneur should first present his successor to the executives. The other employees were to be presented with the successor at a separate company meeting [24].

This gives the successor the opportunity to present himself accordingly and to present his presentation. In addition, the successor should be guided through all areas or departments. Employees should be approached in person at their workplace at this stage and given the opportunity to contact the successor directly. In the end, a similar approach is being taken about customers, suppliers, and the bank.

A heavyweight of the introduction of the successor should lie on the with the different interests in the company.

The importance of the involvement of company managers and employees has already been described. Especially in the context of the introduction of the successor, the involvement of managers and employees is important to avoid the impression of a top-controlled thing. The involvement of employees leads to this. That the new owner can get an idea of his company. At the same time, it is possible to address (new) orientations in terms of content. The more identification is generated between the company, employees and managers and the new boss during the introductory phase, the more successful the cooperation becomes [14].

The development of common visions for the company and employees is of particular importance in this approach. At this point, it turns out that

- -as it stands with the sense of community of the workforce, but also with the new boss.
  - -how and to what extent cooperation is constructive
  - -whether partial interests are marginalized
  - -what skills (potentials and resources) are present in the employees
  - -where resistance to the successor is to be expected.

To make the transition as smooth as possible, it is advisable for the successor to adopt the traditions of the company first, to gently promote the introduction of innovations or to embed them in the traditions of the company.

Finally, the importance of the second level in the company must be recalled. The implementation of entrepreneurial ideas and decisions is determined at this level. There can be a variety of obstacles and defensive postures here. Preventing or bridging these is most likely to be achieved with a strategy of open involvement of the management team in the development of strategies [23].

#### 4.3. Establishment of an advisory board

It may be useful to set up an advisory board in the following cases:

- -If the outgoing entrepreneur still wants to gain influence over the company.
- -If the successor is to be supported for a certain period.
- -If a balance between entrepreneur and successor seems necessary.
- -If the course of business is to be monitored for a while after handover.
- -If essential company decisions are not yet to be fully delegated to the successor.

This advisory board should include entrepreneurs, tax consultants, management consultants, legal advisers and, if necessary, a representative of the financing house bank. The Advisory Board should be provided with the appropriate rights in order to carry out its tasks. His decisions should be binding on both sides.

Future Research should validate the results of this article in study in a wider and more detailed setting. It is necessary to add statistical relevant analyses to validate these results and add to the current state of research.

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