



ADVICE AND PLANNING UPDATE

How to build a strong management team

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Key takeaways:

- An appropriate management framework can help the team work more effectively as well as identify gaps in the existing structure.
- Incentive compensation planning and succession planning are two key tools to help ensure the ongoing success of your management team.

What this may mean for you:

- An empowered management team may enhance the value of your business and increase your transition opportunities.

If you were to reduce your participation in your company by 50%, could your management team successfully run the business? What if you were unable to run your business indefinitely?

These questions are key in evaluating the effectiveness of your management team as operators of the company. Why is this important? Business owners rely on key managers to enact the company's mission successfully. This can involve including managers in setting strategy, executing the strategy through the division of labor, and coordinating to accomplish key tasks.

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Clearly separating the owner and operator roles in your business reduces conflicting priorities and improves your transition options. By having a strong management team in place, as well as a plan to handle any disruptions in management, your management team can be the primary “operator” of your company, thus enhancing your company’s value and expanding your options for potential business transitions in the future.

The first step: Creating a framework to assess your organization

In order to begin mapping over operator responsibilities to your management team, it helps to start with a general management framework.

- Owners and management should segment the overall corporate strategy into tasks that are handled by specific roles or groups.
- Coordination among key roles should be developed to allow management to work together to achieve common goals. A structure is needed to define the levels of authority and the flow of information between roles. Typically, most companies adopt functional divisions (for example, sales, finance, manufacturing, etc.), where the heads of each function work together to set corporate policy.
- Oversight of the divisions is facilitated with systems to monitor company health and enable operations. Systems are important for measuring performance in order to tie managers to specific goals.
- The management team sets the tone for the culture of the company. Their management style and establishment of a shared outlook can impact how individuals work with each other and with customers.

Going through this exercise can also highlight any gaps in the existing structure, such as the need to augment management (for example, hiring a CFO) or adjust responsibilities held by current positions. Creating contingency plans can help address potential disruptions due to the departure or retirement of a key leader. Incentive compensation planning and succession planning are two key tools to begin addressing these issues.

Are you using incentive planning to retain and attract talent?

Incentive planning for the closely held business can answer key questions:

- Does the current compensation plan appropriately incentivize managers toward achieving company objectives?
- Does the current compensation package attract, reward, and retain key employees?

Benchmarking the company’s compensation plan on a regular basis versus those of the industry or geography can identify shortcomings and help attract top talent.

How are you developing resiliency through succession planning?

When a key executive leaves, the company may face numerous risks, including the loss of specialized expertise, a disruption in customer/vendor relationships, and a decrease in employee morale. Succession planning helps minimize the company’s risk exposure by reducing attrition and ensuring business continuity.

Start the planning process by identifying those positions of key importance. Understanding the requirements of the position and the characteristics needed to be successful can help develop a profile of the role. Based on the

profile, interim leaders from other positions within the organization can be identified. If there are gaps of knowledge that must be overcome, the creation of a development plan to prepare successors should be created. Regularly updating the succession plan can keep the company prepared for any surprises.

Ways to enhance the value of your business in a transition

By empowering management, you can prepare for your transition out of the business. A strong management team that can run the company in your absence opens up pathways for a successful transition.

- A management buyout becomes a strong alternative to a retiring or passive owner, especially with a motivated executive team. Such an alternative can also serve as a retention strategy by minimizing risk to managers compared with a new owner while enticing key executives with ownership.
- Sale of the company to an employee stock ownership plan (ESOP) can also reduce risk relative to a new owner. Additionally, it offers all employees the opportunity for ownership in the company while retaining the ability to competitively compensate key managers.
- A strong management team increases the value of the company in the eyes of private equity buyers who are looking to back successful operators. If an owner can demonstrate to the private equity firm that the company can run without their presence, then this may give the owner the opportunity to exit completely from operational roles and possibly reduce any rollover investment into the company going forward.
- A sale to a strategic buyer can give an owner a clean exit while offering management team members the opportunity to advance in a larger organization.

These planning exercises can help you empower your management team to become successful operators of the business. For more information, contact your advisor.

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