



## **Creating A Successful Perpetuation Plan**

Larry G. Linne

An agency owner called me last week and we discussed his recent solicitations from some of the big consolidators and national companies acquiring agencies. He said he has been telling them he isn't ready to sell, but has asked each one, "What would make my business most valuable to you if and when I was ready?"

The summary of the answers from these buyers was: to have a unique and valuable product that the buyer doesn't already have, have leadership that gives confidence to the buyer that they can keep running the company, have talent that performs, and show profit growth. This feedback suggests that the people create the value and, to some extent, are the value of a great company.

My experience, supported by this feedback, makes me believe a highly effective personnel plan will increase the financial and intrinsic rewards to an exiting owner. Without talented leadership, emergency planning, personnel development, and an ownership culture, a financial perpetuation plan could be a waste of time.

### **TALENTED LEADERSHIP**

On my desk I have a sign that says, "CEO's are the number one reason why an agency will not grow." This is there to remind me of how important it is to help agency leadership be effective. The majority of agencies I have worked with have people in leadership positions that would not even be considered for an interview if they applied for their existing job at another agency. Our industry is filled with people that have moved through the ranks and are now leading companies much bigger than they are qualified or trained to lead.

Okay, I am not an advocate of firing all the inadequate leaders. These are great legacy people and they have done a great job of getting us where we are today. However, they are not going to take us to 30% to 40% growth. It takes someone who understands a larger business and knows how to get the agency to the behaviors and processes of a bigger firm. We are often hiring and training future leaders to run our current company, not the one we want to become. If we are developing internal people to become our future leaders, they need external experiences. Otherwise, we need to find people from the outside with skills, knowledge, and experience of bigger firms. Once we find this talent, we need to help our legacy leaders with internal or external job changes.

Leadership is important to the process of internal perpetuation because of the simple fact that the business will be purchased with future profit. If the future leadership can't lead the company to increased profit, the company will have to be sold to a third party. We suggest building a short and long-term plan to get the right leadership in place and put them in the right training to help them lead the business toward becoming a bigger company.

## PERSONNEL DEVELOPMENT

Employees should be evaluated on an annual basis for the value they bring to the organization. This is important because we have to make sure to protect the greatest asset of the business—the people. We need to understand what impact each employee makes on the company and our profit. When we get this clarity we are able to build a plan.

We believe an agency should categorize its employees into four groups:

**Key Employees**—Employees that impact the value of the company. The primary measurement here is the impact they would make if they left the business. Retaining key employees past your exit will impact the value you get for the business. The worst thing that can happen is for a key employee to leave prior to, or at, your exit. We have seen this happen and it can be devastating. Also, the longer you wait to engage a key employee with ownership or financial rewards that tie them to the business, the more it could cost.

**Important Employees**—Employees that have great value to the growth and profit of your business but could be replaced. It may be hard to replace them or the job they do. You could replace them over a period of time but a buyer wouldn't discount the business if they were no longer there. These employees need good compensation plans to motivate performance and retention.

**Valued Employees**—Good quality employees that do a good job. These are the people who are doing the day-to-day work toward your goals. You value them but you could find someone to replace them if needed. These employees need quality HR systems and a great place to work.

**Poor Performing Employees**— Employees not performing. These employees negatively impact your profit and that will decrease the value of your company. Help these employees quickly improve or move them out.

Key employees are the priority. Start an exit plan by developing ownership and compensation models to guarantee you never lose them. We have seen internal perpetuation plans destroyed because of the loss of a key employee, or the key employee became too powerful and valuable before they locked them into a plan. All employees are not equal when it comes to exit planning. Make this a priority and an exit plan will be much more successful.

## EMERGENCY PLANNING

Death and disability are unfortunate potential realities in business that must be considered in a perpetuation plan. In the past few years I have seen three business owners whose untimely deaths caused serious perpetuation problems because not one of these owners had financial or leadership plans in place to help continue the business.

One of my clients does an outstanding job in this area of his business. Jeff Cavnag, from Cavnag and Associates, writes a letter to his partners every year. He calls it the "Mack Truck Letter." The message starts with, "If I were to be hit by a Mack truck on the way to work today ..." He includes all his job duties, suggests who could do those jobs, and gives other instructions they would need to perpetuate

his position. He also gives directions as to who the key advisors are in the business that should be consulted during the transition.

A good perpetuation plan will address every reasonable possibility of unplanned events. Making sure job functions are replaced and the stock repurchase is funded will increase the chance of meeting your perpetuation goals.

Don't allow an unplanned event to completely destroy personal estate plans or legacy plans for the business.

## **OWNERSHIP CULTURE**

The legal profession has done a much better job of bringing in future partners than we have in insurance. They hire people with the expectation that they will become a partner someday. From the start, new attorneys begin working and saving for the opportunity to purchase stock. They know they have to build a client base, revenue for the firm, show leadership skills, and have assets to purchase stock. They are educated early in their career about the stock value and price and are given clear expectations of what it is going to take to get the invitation of ownership.

Our industry has a dysfunctional way of bringing people into ownership. When we hire, the future owner does nothing to prepare for ownership (financially or behaviorally). When we ask them to join ownership they typically don't have any money and they have very little or no understanding of agency ownership and leadership skills.

If a firm is committed to internal perpetuation, it should be hiring future owners, not just producers and managers. This means hiring people with the expectation, but not a guarantee, of ownership. They should be trained on the finances of the business and given clear expectations of how they will come up with down payments or full payment with a bank loan. We should have a clear path to ownership and give them clear instructions on what will be expected of them to become an owner. We should interview them with the thought of being a partner with them some day in the future. A firm that hires future owners and puts them on a specific plan to grow the book, create personal net worth, develop leadership and financial acumen, will have people motivated to a bigger purpose in sales and performance.

The chance of internal perpetuation will dramatically improve if we have an ownership culture. The future owners will never have to change the way they think. They will walk in the door with the thought of ownership as opposed to having to address it many years later.

An ownership culture is one in which people are working toward ownership, and they act like owners before they actually become one.

## **FINAL THOUGHTS**

A financial perpetuation plan can look really good on paper. But, if plans for personnel and leadership are not in place and managed, it becomes a wasted document when you exit. We suggest having a personnel and leadership plan in place years before you plan on internally perpetuating the business.