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# DEFENDER

The National Association of Dealer Counsel Newsletter

MARCH 2015



## Planning for the Future of Family-Owned Businesses *Counseling the Founder*

By Leo M. Garonski  
*Garonski Law, P.C.*

Business and legal advisors understand the importance of succession planning not only to preserve wealth and family harmony, but also to sustain family-owned businesses. What is not widely discussed is the inescapable fact that a change in business leadership will occur whether the owner is prepared or not.

A Harvard Business Review article, “Avoid the Traps That Destroy Family Businesses” (<https://hbr.org/2012/01/avoid-the-traps-that-can-destroy-family-businesses>), reminds us of the familiar aphorism, “Shirtsleeves to shirtsleeves in three generations” that describes the propensity of family-owned enterprises to fail by the time the founder’s grandchildren have taken charge. Authors Stalk and Foley tell us that “The data support the saying. Some 70% of family-owned businesses fail or are sold before the second generation gets a chance to take over. Just 10% remain active, privately held companies for the third generation to lead.”

### Succession Planning – Getting Started

Introducing a succession planning discussion is not always easy. The subject is a confusing and emotional one, because it mixes business and family dynamics in a manner that invariably affects the future of both.

There is a good chance the founder will outright reject, or simply defer, the appointment of a potential successor. In many cases, the founder is skeptical that any of his or her children have the know-how or determination to run the business and lack his or her passion, work ethic and experience, which is often true. In other instances, the founder may be ready to move on to retirement or another interest but may not know whether to:

- Choose a successor from family members or from employees;
- Use a search company to locate a candidate for the job;
- Form a strategic partnership; or
- Sell the business, possibly to a competitor, although selling the business will mean terminating the “family” business and can invoke significant tax implications.

### Opening the Discussion

To begin a succession planning discussion, a neutral environment away from the business helps cultivate an honest, genuine conversation without the pressure of day-to-day operations.

When you ask the founder of a family business whether he or she has given thought to succession planning, in almost every case, the answer is, “Yes, but, the myriad options and the consequences of choices are perplexing.”

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## Typical Questions on the Founder's Mind

*"If my children are involved in the business, should I discuss succession planning with them as a family matter or should I make the decision myself? After all, I have already created enough wealth in the family business that I might want to sell it to preserve the value for the benefit of myself and my family."*

*"On the other hand, my children may have an interest in carrying on the business, but do they have the 'right stuff' to manage my business in an increasingly competitive environment? If my children take over the business, what kind of revenue stream could my spouse and I expect for the rest of our lives? Would we over-burden the family business to preserve our existing lifestyle?*

*"If my children want to continue the business but I still decide to sell it, will I hurt feelings in the family or create differences among our children? After all, I will have to compensate the children who work for me in the family business, but won't pay those family members who didn't choose to work in the family business."*

## Responding to the Founder's Quandary

An advisor is often the first person to ever hear the founder's unvarnished thoughts on the subject, so be prepared to ask good questions and listen intently to the founder's goals.

The best response to the founder's quandary is to assure him or her that the varied options can be viewed in a logical way and the consequences of each option can then be discussed and evaluated.

While the preservation of family wealth is an important issue, transferring a family business to future generations has many benefits. The founder can improve the company's chances of surviving with a new generation of handpicked leaders and two, three, or more generations may benefit from his or her vision and largesse.

## Effective Succession Planning Helps Preserve Family Harmony

As the great-grandson of a company founder who created jobs for generations of family

## Counseling Auto Dealership Founders

Automobile dealers are among the most hard-working and driven entrepreneurs. The highly competitive nature of the auto industry combined with the pressures of sales quotas, manufacturer issues and, economic trends cause dealership owners to focus almost obsessively on their businesses. Few people familiar with the industry would dispute that an automobile dealership is an extension of its owner.

The intense personalities of auto dealers make them challenging clients when dealing with an issue such as succession planning. Considering the experience and perseverance required to earn a dealership badge, it is no surprise that succession planning is such a difficult process for them. Normally decisive in everyday business affairs, a deliberative process with major personal and financial implications can stymie them.

Given the years of experience and hard work typically invested in a dealership, who could blame owners for questioning the knowledge and ability of a child to succeed him or her in the business?

One dealership owner I represented in my legal practice agonized over his succession decision. He wanted nothing more than an ongoing family business, but he could not envision any of his children succeeding without him. After much consideration, he decided to sell the dealership businesses to a competitor and keep the property for an ongoing rental stream of income. Although his decision was successful from a financial standpoint, it caused hard feelings among his children who had worked in the dealerships. While the children received distributions from the sale transaction, they were unhappy to be out of their jobs.

Unlike other industries, rarely are family members and other employees asked to stay with an auto dealership once it has been sold. A new owner usually has a new team in place and a distinct culture.

Mapping out a plan, whether it involves transitioning leadership to someone in the family, selling the dealership and making provisions for wealth distribution or forming a strategic partnership or merger, is a critical decision that is better acted upon sooner than later.

members and effectively contributed to private school and college tuitions nearly one century later, I understand the issues. By passing along the family business, my great-grandfather kept generations of descendants more comfortable than they might otherwise have been —a blessing for which my siblings, my cousins, and I will always be grateful. On the other hand, the multi-generational transfers of ownership were done without

effective succession planning and, therefore, were combative and divisive. There was always a price to pay in family harmony, which better planning and communication could have alleviated. I grew up thinking it customary that relatives threatened each other or cut communication for years over business disputes. Such are the consequences of the failure to plan properly and anticipate family and business issues.

## Leadership Transition – a Competitive Strategy

Personal exposure to family squabbling has given me a firsthand perspective and instilled a passion to help family businesses succeed in handling this often-challenging transition of leadership.

An advisor's job is fourfold:

- To help clients understand that succession planning is a competitive strategy for the business that we can develop in a straightforward manner;
- To counsel them on all succession planning options;
- To map out a strategy that best accommodates unique objectives; and
- To consult the founder's estate planners and tax advisors concerning the impact the plan will have on estate and tax planning.

## Building a Founder's Legacy

While avoidance of succession planning is understandable from a human and emotional perspective, it is important to keep in mind failure to embrace strategic planning can be much worse than the loss of some family wealth.

Family-owned enterprises can avoid the dire consequences of no planning and burnish a legacy to a rich shine whether it is by preparing the next generation for continued success, by selling the company at a great valuation or entering into a strategic partnership.

And, remember, there is no right or wrong goal in strategic succession planning, only that there is a way to make the transition happen, when the timing is right. ■

*Leo M. Garonski is an authority on business and succession planning. As a lawyer for more than 30 years, he has represented private and public businesses in a variety of matters. Because of this experience, he has unique insights into business lifecycles and the secrets of business longevity. It is an interest generated by his personal experience in his own family's business. Mr. Garonski practices in Pennsylvania and New Jersey and has a separate consulting business specializing in succession planning. Email: [Leo@lmgbusinessconsultants.com](mailto:Leo@lmgbusinessconsultants.com)*

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# State of the Automotive Buy/Sell Market Today

By Kenneth R. Rosenfield, CPA

*Rosenfield and Company PLLC*

*Offices – Orlando, New Jersey, Manhattan*

Feature Article

The automotive Buy/Sell Market in the United States has been in high gear over the past twelve months. Although the mammoth acquisition of the Van Tuyl Group by Berkshire Hathaway has stolen much of the news, single point store and other multi-location dealership sales are seeing great activity. Prices and brands are across the board and all over the globe!

From our perspective, institutional investors, including publicly held companies, private equity groups, and fund-backed organizations, are paying higher amounts for Blue Sky and seeking to acquire critical mass in major markets. As their cost of funds is typically lower than private investors, and they may have amassed stockpiles of cash, they are typically looking for a return on investment over a shorter period of time or rapid increases to their stock or portfolio value. It appears that they are also concentrating on the currently better performing brands such as Mercedes, Audi, Chrysler, Hyundai, and Ford.

By no means are transactions among the privately held dealerships at a standstill! There are plenty, if not more dealerships available in all markets. These transactions are more along single point dealerships or smaller groups, both in major markets and in outlying markets to metro areas. One reason behind these transactions is succession planning has come to a standstill within the dealership and the only strategy is to sell off to another group. We have seen many transactions among former competitors or friends. Another consideration is the dealer is fatigued with the business and sees this time period as the opportunity to maximize the value of their franchise.

What are buyers paying for dealerships? Although in some cases we are seeing Blue Sky values at high amounts, there are many bargains available as well. The numbers vary greatly, and the traditional multiples used before are seeing less validity than before. Buyers today are more concerned with units in operation, return on capital required (including investment in facility upgrades and requirements), Customer Satisfaction and Loyalty indexes, market share, and opportunity for improvement. We are increasingly seeing the second or third generation of dealers are remaining employed by the buyers or retaining some small percentage or ownership in the property.

In our experience geography is not as much of a factor. We have been involved in transactions from New England to Missouri to Chicago, and single point domestic franchises have not commanded big multiples as they did in the past. Even small venerable Toyota dealerships have only been able to obtain low end multiples in certain markets. Many of these transaction have been new dealer entries into the business by



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smart investors looking for “starter” stores in markets within 30 miles or less of major metropolitan areas such as Chicago and New York City. These investors have found “deals” that allow them to enter into the industry at price levels which allow a substantial return on investment. The Southeast Corner of the US still has some interest for cold weather investors, but transactions are plentiful across the country.

What is really interesting is the approval rate of the manufacturers in these instances. Rather than the old line of being brought up through the dealer ranks or through dealership training, investors with substantial business experience and success are finding themselves qualified to own a major franchise. This is a relatively new turn for the manufacturers not seen in many years. Now, strong business acumen coupled with significant capital and a solid business plan is getting attention, and dealerships. It cannot be overemphasized the importance of a business plan equipped with what the manufacturers want to see along with capital in obtaining a major franchise and brand.

It is also important to be prepared. Have your books and records in order. Clean schedules and reconciled statements are crucial to improving the value of your dealership and making it more attractive for buyers. Inspecting the books and records is a crucial aspect of due diligence and it sets forth the seller’s best appearance.

Due diligence is just as important as ever, but it is changing from what it used to be. With the rise in facility requirements, both the

sales frontage and service departments in upgraded stores have new and improved equipment and do not require any more investment, at the moment. Older facilities now require a study as to the cost to bring them up to factory standards. More due diligence is required now on the assembled workforce and what it takes to maintain and keep the good employees. In smaller outlying stores, it is necessary to ensure that all of the certifications for the mechanics are up to date, that all of the special tools are in place, and that the goodwill in the customer base is solid and loyal. Where these are not the case, the Blue Sky values are greatly diminished.

Which brands are most favorable? The ones that are available! Most brands are commanding attention although some are not so attractive. It is easier to state those that are least desirable which in this author’s opinion are Buick/GMC, Mitsubishi, and Volvo. These brands are seeing some activity but mostly as “tuck ins”; however, some investors are willing to take a chance on Volvo. Brands coming on the radar seem to be Nissan and Kia (although it is more difficult to generate profit in these dealerships) with the German, luxury brands, and bigger domestic dealerships still leading the pace for highest price. For the non-institutional investor, the domestic and second tier Japanese brands, along with Hyundai and Kia, are bringing a good return on investment and value. In an off note, there has been keen interest in open point Maserati dealerships. We shall see .... ■

## NADC Topical Practice Groups



In accordance with the NADC Strategic Plan the Board of Directors has decided to activate the following two topical practice groups:

- \* **Regulatory Compliance**
- \* **Consumer Litigation**

If you are interested in being involved in either practice group, please contact:

Erin Murphy at [emurphy@dealercounsel.com](mailto:emurphy@dealercounsel.com).

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## President's Message



Oren Tasini

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This is my final President's Message. A new President will take office at our April meeting in Laguna. I am hoping that many of you will be in attendance. As a founding member of the NADC, it has been my privilege to serve as President these past two years. Many thanks go out to our Executive Committee, our Board of Directors, and our Executive Director Erin Murphy. All these people made my job easy. When asked, people volunteered without hesitation and then completed the tasks needed to keep the NADC vibrant and growing.

But an organization is only as good as its members, and to each and every member, I give my heartfelt thanks for your participation and membership in the NADC. We continue to grow and add members and it is members who provide the most valuable component of NADC: the shared knowledge of lawyers who represent dealers. I would be willing to bet, and I am not a betting man, that any member asked would say that having the access to other lawyers with similar legal problems and issues is the most valuable feature of the NADC. Our seminars are a testament to the high level of expertise and proof that the NADC has become what we envisioned upon its founding: a valuable resource for those of us seeking to represent dealers in a challenging regulatory environment. I hope, that like me, you are proud to be a member of NADC and receive more from it than you put in.

As Past Presidents have noted, and whose sentiment I echo, I hope that I have left the NADC stronger than it was when I took on the mantle. I thank you for your support and look forward to my continued involvement in NADC as it grows and prospers. ■



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