



2009 National Conference For Community Bankers

SUCCESSION PLANNING: Preserving Legacy and Harmony Family and Closely Held Banks

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Overview of Today's Discussion

- Why Succession Planning is so Important
- Considerations for Family and Closely Held Banks
- Succession Planning: Tips on Process
- Case Study/Discussion/Q&A/Audience Sharing

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Why Succession Planning Is So Important

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Why Talk About Succession Planning?

- One of the most critical responsibilities for companies today
- Ranked a top issue by National Association of Corporate Directors (NACD)
 - 2006 – 2008 NACD Governance surveys
 - Includes all companies – public and private
- Fewer than half of companies (both public and privately held) rated succession planning process as effective
- Many companies do not have a CEO succession plan in place
 - Only 57% of public companies
 - Only 33% of private companies
- A major concern in today's environment:
 - CEO tenures are down, with 40% of top leaders failing in first 18 months
 - Highly competitive and challenging business environment
 - Aging workforce – many "boomer" retirements
 - Internal development of "high potentials" often haphazard
- More challenging in a family/closely held business
 - "Insurance" for the future continuity of your business and future generations
 - Encompasses broader succession issues (family leadership/ownership, governance, and key management)

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Consider These Statistics

From The Family Business Institute:

- 4 out of 5 family businesses are still controlled by their founders
- > 50% expect their companies to change leadership by 2013
- ~ 1/3 have a CEO who is older than 60
- 88% believe the same family will control their business in five years
- BUT, only 30% of family businesses survive into the second generation, 12% into the third generation and only about 3% into the fourth generation

From the U.S. Small Business Administration:

- 90% of the 21 million small businesses in the U.S. are family-owned, but only 30 percent of family-run companies succeed into the second generation, while only 15 percent make it to the third
- Only 1/3 of closely held business owners have a formal plan to sell, transfer or hand down their business in the future

The Nay Sayers:

- The Firefly phenomenon
 - Flicker for a brief moment, then die away
- Rule of the "Thirds"
 - One third of businesses make it to a second generation, a third of those live to see a third generation, and so on... ("shirtsleeves to shirtsleeves")

Why Talk about Succession Planning?

WHY SO DIFFICULT? Procrastination Too busy Can't imagine the need No one else can fill shoes Who wants to think about their death or disability? Don't know where to start Easier to be reactive No family member takes responsibility	WHY SO IMPORTANT? Retirement Termination Resignation Personal crisis Death Disability Industry change M&A Governance requirements Regulators are watching
WHO CARES? Customers Community Partners Employees Family Members Non-Family Key Management Regulators	WHAT HAPPENS IF IT DOESN'T EXIST? Loss of continuity Stress on business Reduced employee morale Lost productivity Loss of business Negative impact on revenue Close of business Sale at inopportune time

Family Enterprise Succession Planning

- Family enterprise succession planning objectives are similar to mutual/public banks....
 - Seamless transition of leadership of business
 - Align with future needs of business
 - Managing multiple perspectives
- But different in other ways....
 - Seamless transition of family and business leadership
 - Align with future needs of the business and individual/collective needs of family/owners
 - Ensure liquidity for retiring generations
 - Integrate estate planning with succession planning
 - Maintain and preserve family capital
 - Balance business needs with family values
 - Maintain family harmony and engagement
- Family enterprise succession planning encompasses management, governance ownership and estate planning/tax management
- Goal is to provide the family/owner with a vision of what their enterprise ownership and management will look like in the future and a plan for making it happen smoothly.

Successful Transition is Process Not an Event

Can You Answer These Questions?

- ✓ Do you have a succession plan? (More than a single page or scratches on a napkin?)
- ✓ Who is responsible for CEO Succession at your bank?
- ✓ Who is responsible for Board Succession at your bank?
- ✓ Who is responsible for family leadership succession?
- ✓ What is your process?
- ✓ Do you monitor your talent base?
- ✓ Do you have a process for developing strong leadership “bench strength” (Family/Non-Family)?
- ✓ What are your “gaps” on the team?
- ✓ How do you make succession decisions?
- ✓ How do you ensure proper transition during change?
- ✓ What would you do if your CEO did not return to work tomorrow (death, illness, lottery)?
- ✓ What is the CEO's plan for retirement?
- ✓ Do you know who your CEO considers their successor? Who your Board considers the CEO's successor?
- ✓ What criteria are you using for selecting successors (CEO, Board, Family Leadership)?

Succession Planning Considerations For Family and Closely Held Banks

Aligning Family/Owner Strategies with Bank Strategies

- Succession planning IS strategic planning
 - For banks, people are your business
 - Your future success depends on your future leaders (family and non-family)
- Aligning leadership needs with the future vision strategy and goals for the bank is critical to viability of company
- Critical issues for family/owners: Parallel Planning
 - Coordinating strategic planning processes – business and family
 - Objective – unify ownership, board and management in support of common direction
 - Succession planning is an outcome of good parallel planning
- Parallel Planning: Ownership, Board, and Management
 - Agree on goals via shared inquiry and informed dialogue
 - Establish and execute strategic plan
 - Monitor results and require accountability
 - Key players – family leader, board chair, CEO
 - Key question (how to balance growth, profitability, liquidity, risk)

Engaging Family Members as Informed Owners

How have families been successful in building sustainable family enterprises for the long term?

- By establishing family agreement on principles of informed and engaged ownership
- By transforming these principles into action by board and management
- By assuring that succession is in place for key positions (family, board, key management)

How have enterprising families accomplished this transformation successfully?

- By creating a charter for family enterprise(s) which commits to long term focus, emphasizes family values, and incorporates basic principles to be followed
- By establishing structures, processes, criteria (formal or informal) which support and build on these principles
 - **Education** – To encourage all family members to be informed and engaged owners
 - **Competency development** – To build and maintain requisite competencies for family board and management (also for family members wanting to be Board Members and/or Management)
 - **Agreed upon criteria** – For family leadership, board membership, and enterprise management
 - **A nomination/selection process perceived to be rigorous and fair** – For family leadership and Board Membership

Building and Maintaining a Strong Board of Directors

What have successful enterprising families done to build a strong Board of Directors which provides oversight and guidance to management aligned with ownership direction?

Examples from successful enterprising families

- Agreement that the board will select well qualified family and independent non-family Directors
- Family member chair of the board and governance committee
- CEO (family or non-family) hired and evaluated by board
- Board in charge of CEO succession process
- Established structures, processes, criteria for governance leadership selection and evaluation
 - **Family** – Selects family members for Board positions
 - **Board Governance Committee**
 - Nominates both family and non-family board members from a pool of well qualified candidates
 - Evaluates board performance, sets criteria and benchmarks
 - **Board and Governance Committee** – Governance committee nominates committee chairs, board selects committee chairs

Building and Maintaining Strong Key Management

What steps have successful family enterprises taken to build and maintain strong key management?

Agreement by ownership and by Board that qualifications for enterprise key management positions trump family entitlement

- CEO – Selection, evaluation, and criteria for selection are the responsibility of the Board – subject to dialogue with family leadership (parallel planning)
- Key Management – Selection, evaluation and criteria are the responsibility of the CEO – subject to Board oversight

Questions for ownership and Board of Directors

- What should be family employment policy? Tie goes to a family member?
- What should be the enterprise policy for mentoring family employees?
- What enterprise-wide development should be in place to grow family and non-family “high potentials”?
- When should succession process for CEO and key management commence?

Family Leadership Succession

Who is in charge of the family leadership succession process? The Family

Examples from successful enterprising families:

- Designate family leader(s) and provide support (structure can be formal or informal)
- Build and sustain culture that family leadership and unity are very important to enterprise success
- Establish and manage family leadership succession process
- Encourage
 - Development of family members for family leadership, governance, and management responsibilities
 - Service on enterprise board or managing member of family LLC or family partnership can be excellent preparation for family leadership
- Speak with one voice on family enterprise matters
 - E.g. parallel planning

Board Succession – Family Members

Who is in charge of the succession process for family board members? The Board

Examples from successful enterprising families:

Board Chair

- Establish policy that board chair should be a family member
- Family nominates, board approves based on mutually agreed upon leadership criteria
- Key position –
 - Speaks for board to family and to management
 - Dialogues with family and management on direction (parallel planning)
 - Sets board agenda
 - Translates family ownership direction to management on behalf of board
 - Champions CEO Succession Plan and oversees execution

Board Succession – Family Members / Non-Members

Who is in charge of the succession process for all board members? The Board

Examples of how families and family enterprises have addressed this issue:

- Vice Chair – a potential successor to Board Chair
 - Should be a family member
 - Should have substantive responsibilities (i.e. chair governance committee, act as lead director)
- Other board positions important for family and non-family leadership development
 - Board committees
 - Generational and branch representation
- Maintain appropriate representation of qualified independent directors – answer these questions
 - Should there be a majority of independent directors?
 - How large should the board be to accommodate sufficient family and non-family members?
 - What key board positions should independent non-family board members be considered for?

CEO and Key Management Succession

Who is in charge of the CEO Succession process? The Board

- Common themes – CEO Succession
 - Board establishes leadership competencies and timeline
 - Succession process championed by board chair – CEO participates
 - Usually a board committee is responsible to board for managing process
 - Qualified internal candidate normally preferred – (but what if no qualified internal candidate?)
 - When should formal succession process begin?
 - Internal candidates given many opportunities to interact with board
 - Leading candidate identified at agreed upon date
 - CEO and designated successor work together during transition period
 - Retiring CEO gets out of the way at retirement
 - Emergency succession plan should be in place
- Examples of how families and family enterprises address CEO succession when family and non-family members are candidates:
 - Family member CEO to family member CEO
 - Family member CEO to non-family member CEO
 - Non-family member CEO to non-family member CEO

Estate Planning and Succession Planning

How do successful enterprising families view estate planning?

- See as part of an integrated ownership succession planning process
- Maintain perspective - other higher family priorities take precedence over minimizing tax
- Many estate planning techniques available – select wisely

Tax Management basic principles:

- Defer tax to subsequent generations
- Cut tax rate

Estate Planning and Tax Management

Have you considered the following commonly used designed to cut estate tax rate?

- Techniques / Structures designed to cut estate tax rate
 - Maximize \$3.5 million exemption (H + W = \$7 million)
 - Valuation discounts – closely held stock, LLC or limited partner interests
 - Lifetime or testamentary charitable gifts, particularly split interest gifts

- Techniques / Structures designed to defer estate tax
 - Freezing value of senior generation stock (sale to defective grantor trust, “freeze” family LLC or “freeze” family partnership)
 - Lifetime gifts of property likely to appreciate
 - Generation skipping trusts

Succession Planning: Tips on Process

Tip # 1: Engage All Stakeholders

- Family/Board
 - Alignment with family and business strategy/goals (parallel planning)
 - Perspectives and input on criteria for role(s)
 - Input and feedback throughout
- Current CEO
 - Input on role
 - Collaborates in process – doesn't drive it
- Top Management
 - Potential candidates
 - Perspectives and feedback
- Board Committee
 - Facilitates process
- Outside experts
 - Facilitators
 - Recruiters/assessment firms

Tip # 2: It's a Process not a Destination

- Ongoing process; fluid and dynamic
- Not one time exercise to file away – don't let it collect dust!
- Not a product but a process
- Active, ongoing discussions
- Keep eye on potential candidates
- Requirements change constantly – need to continuously adapt
 - Industry
 - Leadership team changes
 - Strategic goals/initiatives
 - Key leadership characteristics

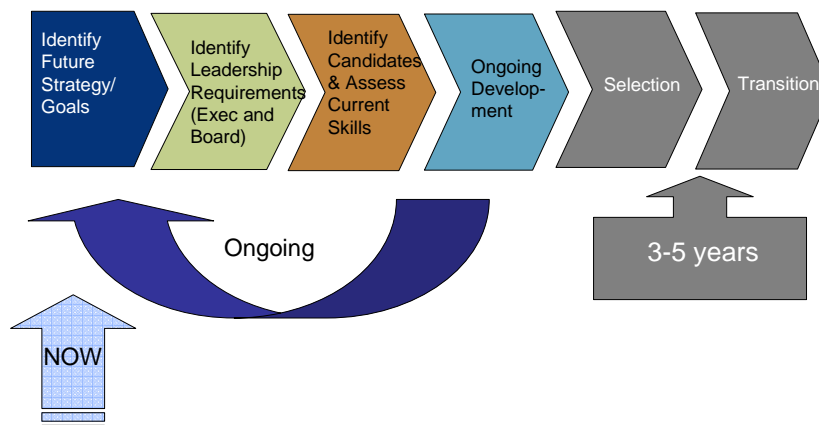
Tip # 3: Start Now!

- Never too early to plan for development
 - Provide time to spot future stars and develop them
- Need to have emergency plan
 - You never know
- Active planning 2-5 years before need (e.g. retirement)
- Ensure proper transition
 - Development of successor candidate(s)
 - New CEO overlap with current CEO
 - Outgoing CEO facilitates transition then “gets out of the way”
- The hard part is starting
- Once the process is in place – it’s easy to update

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A Succession Process



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Case Study/Discussion/Questions