



# Business Succession: Keeping Grocery Stores Alive

## Rural Grocery Store Guide Supplement

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A succession plan, sometimes called an exit strategy, is an outline of how and when you plan to leave your business, what your goals are for the continuation of the business and how those goals are going to be met. For most entrepreneurs a succession plan is far from being a priority. When trying to start a business, the last thing entrepreneurs wish to contemplate is the possibility of closing their business. And, during the life of the business, they are too busy with the day-to-day operations to plan for the future.

However, there are many reasons to make time for succession planning and, for most business owners, the financial planning necessary to ensure stability and comfort in retirement should be considered a top priority. Also, for many business owners, carrying on their legacy is very important. They hate to see the business they've spent years building being dissolved at their retirement. Finally, the community stands to lose an important asset (jobs, tax revenue, and access to fresh food) if the business closes because of a lack of planning. This last issue is very important when it comes to rural grocery stores.

### **Saving for Retirement**

Part of succession plan includes planning for the financial needs of the owners after they exit the business. The sooner this is addressed the better. There is no 401K or company matched savings account when you work for yourself. In some cases the company can build equity in assets that hold value such as real estate or large equipment. But many owners plan on using the proceeds from the sale of their business to fund their retirement and support their lifestyle for the rest of their lives.

Unfortunately business owners often over estimate the value of that business and it is important to start planning and saving toward retirement as early as possible and to save consistently over the years the business is active. In general, in the early years of saving for retirement, owners can tolerate more risky investments with higher returns. On the other hand, as owners approach the age of retirement, it is important to invest in more secure ways. For instance stocks might be a good option



if you are 10-20 years from retiring but bonds and money markets might make more sense if you will need the money in a few years. More information on planning for retirement is available from the Small Business Administration (<https://www.sba.gov/content/plan-your-exit>). It is advisable to seek the help of a professional accountant or financial adviser with both retirement savings and estate tax issues.

## Business Valuation

Business valuation is a very complicated subject. There are several methods of arriving at a value, and a professional appraiser will look at a couple models to arrive at a value range. An appraisal by a professional can be fairly expensive for a small business owner but the appraisal can add to the value of the business and ease the financing for a buyer, making the sale quicker and more profitable in the long run.

If an appraiser is not used the sale will be limited to either the amount the lending institution agrees to (usually based only on long term assets) or the funds the buyer is willing to pay and able to raise on his/her own.

## Specific Situations in Succession Planning

While every situation will be unique, the following is a discussion of a few of the more common scenarios that occur when an independent business person decides it's time enter a different stage in their life.

### *Leaving a Partnership*

In general, the dissolution of a partnership is relatively straight forward, provided that the parameters of the partnership are outlined well, that the value of the partnership is known and that the end of the partnership is not unexpected.

Once the valuation of the partnership is established and a decision made as to the percentage of ownership each partner has, it is important to plan for an unexpected departure by one of the partners (e.g., a sudden death). This is most commonly done with life insurance and there are two main ways of structuring this from the businesses stand point. The first is called a "cross-purchase agreement" in which the partners buy and own a policy on each other. When one partner passes away the remaining partners collect the insurance and use it to buy out the deceased partner's share of the business from his/her estate.

The second option is an "Entity-Purchase Agreement". In this case the insurance for each

partner is purchased by the business itself. From here it proceeds exactly like a "Cross-Purchase agreement". The business itself collects on the policy and uses the proceeds to buy out the deceased partner's share of the business (Investopedia 2014).

### *Closing without a Sale*

To close a business without sale can be quick, but the owner often loses income. Usually all that is recouped is the price of the used equipment and a clearance on any inventory that can be sold. If there is real estate involved there may be a more substantial sum from its sale. However, any value from years of building a client base and a well run operation with a well-regarded name is lost.

The State of Illinois' tax website (<https://mytax.il-linois.gov>), and the federal website (<https://www.sba.gov/content/steps-closing-business>), have additional information on the legal aspects of closing out your business.

### *Finding a Successor*

Finding a successor is different than simply selling your business. A successor is someone you hope will take your business to the next level. It might be a family member or a trusted employee. With business succession come a host of issues because of the relationships and emotions are involved. Succession planning involves not only the present and future owner(s), but also their family members. At a minimum, succession planning includes identifying a successor, establishing goals and objectives, establishing a decision-making process, estate planning, and choosing the form of the transition.

*Identify successor(s).* This may be a family member, a trusted employee, a customer or supplier, or even a young person in the community who has an interest in your business. It may also be a consumer cooperative, worker cooperative, or community-owned corporation formed for the purpose of purchasing and operating the grocery store. Begin discussing your plans for transitioning the business with potential successors to gauge their level of interest and qualifications. The process is not that different from that of recruiting any new employee. Once a successor is identified, bring them into the business and give them an appropriate level of responsibility so that they can learn about your store and develop a sense of ownership in the business.

*Establish Goals & Objectives.* To ensure success, is vital that everyone involved in the transition

(present owner(s), future owner(s), family members, and employees) share the same vision for the future. Therefore, the present owner(s) and future owner(s) must work together to develop that vision as well as concrete goals for the business. The owner(s) must also establish clear retirement and cash flow goals for themselves and any family members dependent on the business. The role, if any, of those family members in terms of a continued involvement in the business must be clarified. Finally, the future owner(s) should identify their own goals for the future, including income goals and work/life balance goals. It is also a good idea to revise the existing business plan and financial statements.

*Establish a Decision-Making Process.* Until the final “handover” of the business, it can be unclear who has authority for business decisions and disputes can result. These disputes can derail even the best plan. The present and future owner(s) must establish a clear decision-making process that includes a method of resolving disputes and spells out the role, if any, of family members in decision-making. This plan should be documented in writing and communication to family members, employees, and other interested parties.

*Create a Business and Owner Estate Plan.* Selling or transferring ownership of a business can have tax implications for the owner and the business; however, careful planning can minimize these implications. It is in the best interest of both the current owner(s) and the future owner(s) to work with an attorney or accountant familiar with these issues.

*Determine the Form of the Transition.* There are many ways to structure a transition, including an outright sale, a gradual sale, or a gift. A gift may be appropriate with a transfer to a family member and when the present owner can afford to forgo the income of the sale. With a sale, financing can be structured so that the retiring owner(s) receive a steady stream of income over a number of years. Transfer of ownership can also be accomplished through a combination of all these methods (Forbes 2013).

### *Alternative Business Models*

Sometimes it can be difficult to find an individual buyer with resources and experience in rural areas. At the same time, the community would be hurt by the loss of its only grocery store. In cases like this, an alternative business succession process may be the solution. Alternative business models include mutual ownership (including cooperatives), joint venture, or seller financing.

*Mutual Ownership or Cooperatives.* In a cooperative model, the business is sold to a group of buyers who benefit directly from the grocery store — its customers, its employees, or a combination of the two — who then own and operate the business on a one member/one vote basis. Alternative mutual ownership options are available when the specific requirements of a cooperative are not suitable, often involving the formation of a community-owned corporation or LLC in which community members can invest at varying levels. While traditional cooperatives explicitly entail a commitment to community well-being, new social enterprise structures such as the low-profit limited liability company (L3C) model may be applicable for mutually-owned grocery businesses with explicit community betterment purposes. For more information about cooperative and mutually-owned options, see “The Cooperative Model of Grocery Store Ownership” guide in this series.

*Joint Venture.* A joint venture is a situation in which one business entity partners with another business entity to produce a new financial venture. Joint ventures are useful when both parties desire the same outcome but lack the resources to take action by themselves.

For joint ventures formed by small family businesses or single entrepreneurs, it is vital that the ground rules of the partnership be clearly defined or the individual personalities can make it difficult to find business solutions that satisfy all parties. Things like voting power and areas of control must be clearly defined and recorded. One possible example might be a small local pharmacy joining with a struggling local grocery store to share the costs of advertising, building expense, utilities, etc. This could be the boost that either business might need to stay open. But the legal regulations for the two businesses are very different and it is extremely important to make sure that the decisions for each business are made by the partner that has expertise in that field. If regulations are not handled correctly the joint venture can inadvertently violate the law.

*Seller Financing.* The seller financing, or what is sometimes called “lease to own” option is sometimes the only way a business can be purchased from an existing owner. For a grocery store the value of its inventory can be as much as \$100,000 or more. This asset is a perishable good and as such is not normally used by lenders as collateral. This leaves the would-be grocer unable to borrow against this asset and needing a very large amount of out-of-pocket start-up capital. The seller financing option overcomes this obstacle as well as many others associated with traditional financing.

Seller financing does have a downside for the seller, however. If the new owner fails, the seller may end up coming out of retirement to run the store until another buyer is found. It's a significant risk but in many cases it is the only way that the seller may be able to sell the business.

### *Options for Diversification*

A transition of ownership does not require that a grocery store maintain the exact same scope and structure that it originally had. The front of many small town grocery stores do second duty as a seasonal ice cream shop, a demo space for cars or lawn and garden equipment, or an ATM location for a local bank (with the transaction fees shared between the store owner and the bank). In some cases there may be opportunities to add additional food product lines or non-food products and services in order to increase profitability and better serve the local community. In other cases it may be necessary to focus a grocery business more tightly on certain specific product lines. No single option is universally applicable to all rural grocery stores, but a number of options have been explored by rural grocery stores in the Midwest and are worth evaluating.

- Add an indoor farmers market. Outdoor farmers markets have grown greatly in popularity in Illinois, and are a key way to connect consumers to fresh, local food products — but they have obvious seasonal limitations. Bringing the farmers market concept indoors extends the retail season for both consumer and farmers. An existing grocery store may be a candidate to operate or simply physically host such a market. For more information, see “The Indoor Farmer’s Market: Evolution of a Local Food Sales Model” guide in this series.
- Add natural foods product lines. In some communities, access to food products with natural, organic, and other related labels lags behind consumer demand. See “The Cooperative Model of Grocery Store Ownership” for a brief discussion of this strategy, which has been implemented by a number of cooperative grocery stores in Illinois.

- Increase focus on specific artisanal or service-oriented food product lines, such as specialty baked goods or fresh meats. In some cases these segments are an opportunity for a small grocery to offer a product and a retail experience that surrounding larger grocery stores do not.
- Transition toward a convenience store model, with or without fuel sales. In some circumstances a smaller-sized store focused on convenience items may be viable when a traditional grocery store is not. A convenience store format does not necessary need to exclude healthy items like fresh produce.

### **References**

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