

by **Stephen H. Franklin**

Family businesses have more challenges growing

Family businesses have more than the usual challenges to their sustainability and the economic value accumulated inside the business. In this column, I will focus on three ideas:

- Reducing personal financial risk to the owner/operator
- Financial planning to assist with extracting the value locked within the business
- Preserving and growing assets

Reducing risk

The wealth of owner/operators of family businesses frequently is concentrated in a single asset: the business. This asset is neither diversified nor liquid, potentially placing wealth at high risk.

Business owners often reduce some of their risk through insurance to create capital for contingencies, such as death and disability, without liquidating the business in an untimely fashion.

However, steps to reduce the inherent risk of concentrating wealth in a single asset are often overlooked.

One way is to invest a significant portion of income in other assets. Diversifying should help lower risk associated with having a large portion of the owner's wealth invested in his business over the long term. Other choices include extracting value and investing the proceeds.

Business owners and operators should consider using a professional financial adviser to develop an overall investment policy that views the business as one asset in a portfolio that has parameters regarding growth, income and risk based on personal circumstances.

Financial planning

Business owners can get significant value by clearly defining future income needs and capital requirements before negotiating a refinancing or sale of a family business. All too often, business owners start this type of financial planning after they have finalized the financing or sale transaction. Earlier involvement in

structuring a financial plan provides a framework for negotiations.

For example, specifying what income is wanted, determining actual financial need and projecting how long it will be required are the basis for quantifying goals and evaluating alternatives.

Using a structured process will help in weighing alternatives and consequences of the goals that matter most.

Extract value

Capital can be extracted with or without a sale. The choice depends on the situation and goals. An advisory team can explore options including refinancing, selling or going public to unlock the value built in the business. Each alternative will have pros and cons. Planning will help owners/operators decide which choice is most appropriate for the circumstances.

Without a sale, it may be possible for capital to be transferred by dividend distribution.

In addition, the financial and non-financial goals could be well served by taking cash out through refinancing. Most likely, this alternative will provide less cash than a sale and require continued personal management. However, this alternative provides the opportunity to retain control of the operation, values and opportunity for succession. Knowledge of capital requirements will help in deciding alternatives in negotiating the transaction.

Wealth preservation, growth

The combined processes of personal financial planning and investment advisory services provide knowledge and direction for investment decisions. The planning and advisory services are especially important for business owners whose wealth is concentrated in their business and who are contemplating securing their financial needs. Developing an investment strategy for asset allocation and disciplined management will significantly reduce risks and improve the chances of meeting investment goals.

Stephen H. Franklin is a financial consultant with Roof Advisory Group, an independent investment management and financial planning firm based in Harrisburg. The firm is a fee-only Registered Investment Advisor that manages assets and preserves wealth for individuals & institutional clientele. Contact them at 717-260-9281 or by e-mail at roofadvisory@earthlink.net.